

OFICINA DEL COMISIONADO DE ASUNTOS MUNICIPALES
AREA DE ASESORAMIENTO, REGLAMENTACION E INTERVENCION FISCAL
AREA DE ARCHIVO DIGITAL

MUNICIPIO DE GUAYAMA
AUDITORIA 2003-2004
30 DE JUNIO DE 2004

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COMMONWEALTH OF PUERTO RICO

MUNICIPALITY OF GUAYAMA

SINGLE AUDIT REPORT

YEAR ENDED JUNE 30, 2004

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COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA

SINGLE AUDIT REPORT

YEAR ENDED JUNE 30, 2004

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COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA

SINGLE AUDIT REPORT

YEAR ENDED JUNE 30, 2004

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López-Vega, CPA, PSC

Certified Public Accountants / Management Advisors

Member of

- American Institute of Certified Public Accountants
- Puerto Rico Society of Certified Public Accountants

INDEPENDENT AUDITORS' REPORT

**To the Honorable Mayor and
the Municipal Legislature
Municipality of Guayama
Guayama, Puerto Rico**

We have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the **Municipality of Guayama, Puerto Rico**, as of and for the year ended June 30, 2004, which collectively comprise the Municipality's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Municipality's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America, the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, and the provisions of the Office of Management and Budget Circular A-133, *"Audits of States, Local Governments, and Non-Profit Organizations"*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether the respective financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the respective financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statements presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the governmental activities, each major fund, and the aggregate remaining fund information of the **Municipality of Guayama, Puerto Rico**, as of June 30, 2004, and the respective changes in financial position, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

INDEPENDENT AUDITORS' REPORT (Continued)

The Management's Discussion and Analysis on pages 3 through 11 and the Budgetary Comparison Schedule-General Fund on page 37 are not a required part of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued our report dated December 20, 2004 on our consideration of the Municipality's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grants.

Our audit was performed for the purpose of forming an opinion on the basic financial statements of the **Municipality of Guayama, Puerto Rico** taken as whole. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is not a required part of the respective financial statements. The information in that schedule has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly presented, in all material respects, in relation to the basic financial statements taken as a whole.


LOPEZ-VEGA, CPA, PSC

San Juan, Puerto Rico
December 20, 2004

Stamp No. 2019430 of the Puerto Rico
Society of Certified Public Accountants
was affixed to the record copy of this report.



**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA**

MANAGEMENT'S DISCUSSION AND ANALYSIS

YEAR ENDED JUNE 30, 2004

Management's Discussion and Analysis

As management of the Municipality of Guayama, we offer readers of the Municipality's basic financial statements this narrative overview and analysis of the financial activities of the Municipality as of and for the fiscal year ended June 30, 2004. This Management's Discussion and Analysis (MD&A) include comparative data, and it has been designed accordingly with the following goals:

- a) Assist the reader in focusing on significant financial issues,
- b) Provide an overview of the Municipality's financial activity,
- c) Identify changes in the Municipality's financial position (its ability to address the next and subsequent year challenges),
- d) Identify any material deviations from the financial plan (the approved budget,) and;
- e) Identify individual fund issues or concerns.

Since the MD&A is designed to focus on the current year activities, resulting changes and currently known facts, please read it in conjunction with the Municipality's financial statements.

FINANCIAL HIGHLIGHTS

- The Municipality net assets increase by \$ 14,322,542.
- In the fund financial statements, the governmental activities revenue increase \$ 3,754,309 (or 9%) while governmental activities expenditures increase \$ 6,013,175 (or 16%).
- The General Fund (the primary operating fund) reflected, on a current financial resource basis, an increase of \$ 2,025,212.
- On a budgetary basis, actual revenues exceeded actual expenditures by \$ 2,669,199.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA**

MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)

YEAR ENDED JUNE 30, 2004

Using This Annual Report

This annual report consists of a series of new financial statements with a change in the focus from previous financial statements. The new focus is on both the Municipality as a whole (government-wide) and the major individual funds. Both perspectives (government-wide and major fund) allow the user to address relevant questions, broaden a basis for comparison (year to year or government to government) and enhance the Municipality's accountability.

Government-Wide Financial Statements

The Government-Wide Financial Statements are designed to provide users of the financial statements with a broad overview of the Municipality's finances in a manner similar to private-sector companies.

The Statement of Net Asset presents information on all of the Municipality's assets and liabilities, with the difference between both reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the Municipality is improving or deteriorating.

The Statement of Activities presents information showing how the Municipality's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of the related cash flows. Thus, revenues and expenses are reported in the Statement of Activities that will only result in cash flows in future fiscal periods. The Statement of Activities is focused on both the gross and net cost of various activities, which are provided by the government's general tax and other revenues. This is intended to summarize and simplify the user's analysis of cost of various governmental services.

Fund Financial Statements

The Fund Financial Statements provide detailed information about the Municipality's most significant funds, not the Municipality as a whole. The Municipality has only one kind of fund which is the governmental fund.

Governmental funds are used to account for essentially the same functions reported as governmental activities in the Government Wide Financial Statements. However, unlike the Government Wide Financial Statements, Government Fund Financial Statements, focus on near term inflows and outflows of spendable resources, as well as on balances of spendable resources available at the end of the fiscal year. Such information is useful in evaluating the Municipality's near term financial requirements.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA**

MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)

YEAR ENDED JUNE 30, 2004

Fund Financial Statements (Continued)

Because the focus of governmental funds is narrower than that of the government wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the government wide financial statements. By doing so, users of the basic financial statements may better understand the long-term impact of the Municipality's near term financial decisions. Both of the Governmental Fund Balance Sheet and the Governmental Fund Statement of Revenues, Expenditures and Changes in Fund Balances provide a reconciliation to facilitate this comparison between governmental funds and governmental activities.

Infrastructure Assets

Historically, a government's largest group of assets (infrastructure-roads, bridges, underground pipes [unless associated with a utility], etc.) have not been reported nor depreciated in government financial statements. GASB 34 requires that these assets be valued and reported within the Governmental column of the Government-Wide Statements. Additionally, the government must elect to either (a) depreciate these assets over their estimated useful life or (b) develop a system of asset management designed to maintain the service delivery potential to near perpetuity. If the government develops the asset management system (the modified approach) which periodically (at least every third year), by category, measures and demonstrated its maintenance of locally established levels of service standards, the government may record its cost of maintenance in lieu of depreciation. The information about the condition and maintenance of condition of the government infrastructure assets should assist financial statement users in evaluating a local government and its performance over time.

The Municipality elected to depreciate infrastructure assets instead of using the modified approach.

FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE

Net Assets

As noted earlier, net assets may serve over time as a useful indicator of a government's financial position. The Municipality's combined net assets (excess of assets over liabilities) totaled \$ 22,737,141 at the end of 2004, compared to \$ 8,415,199 at the end of the previous year.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA**

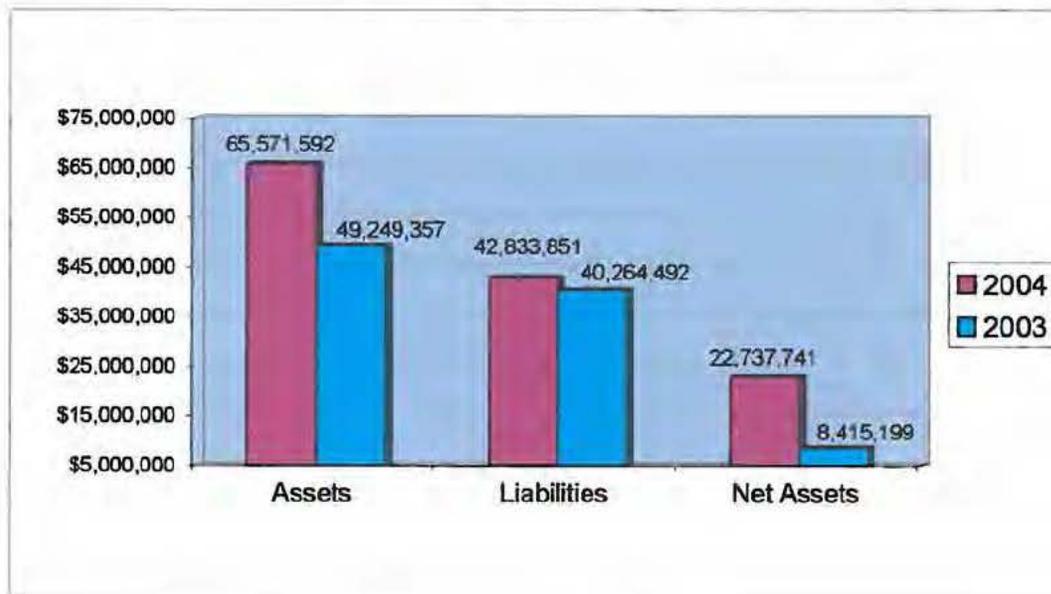
MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)

YEAR ENDED JUNE 30, 2004

FINANCIAL ANALYSIS OF THE MUNICIPALITY AS A WHOLE

Net Assets (Continued)

Condensed Statement of Net Assets	2004	2003	Change	%
Assets				
Current assets	\$30,810,789	\$24,594,021	\$6,216,768	25%
Capital assets	19,119,573	12,116,987	7,002,586	58%
Other assets	15,641,230	12,538,349	3,102,881	25%
Total assets	65,571,592	49,249,357	16,322,235	33%
Current liabilities	8,794,203	8,287,424	506,779	6%
Noncurrent liabilities	34,039,648	31,977,068	2,062,580	6%
Total liabilities	42,833,851	40,264,492	2,569,359	6%
Invested in capital assets, net of related debt	13,351,698	6,577,230	6,774,468	103%
Restricted	19,805,513	15,835,903	3,969,610	25%
Unrestricted	(10,419,470)	(13,997,934)	3,578,464	(26%)
Total net assets	22,737,741	8,415,199	14,322,542	170%



**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA**

MANAGEMENT'S DISCUSSION AND ANALYSIS – (CONTINUED)

YEAR ENDED JUNE 30, 2004

Changes in Net Assets

The Municipality's net assets increase by \$14,322,542. Approximately 41 percent of the Municipality's total revenue came from taxes, while 54 percent resulted from grants and contributions, including federal aid. Charges for Services provided 1 percent and Interest revenue and miscellaneous 4 percent of the total revenues. The Municipality's expenses cover a range of services. The largest expenses were for health and welfare services, general government, public works, and public safety. As follow, is presented a comparative analysis of governmental-wide data. With this analysis, the readers have comparative information with the percentage of change in revenues and expenses from prior year to current year.

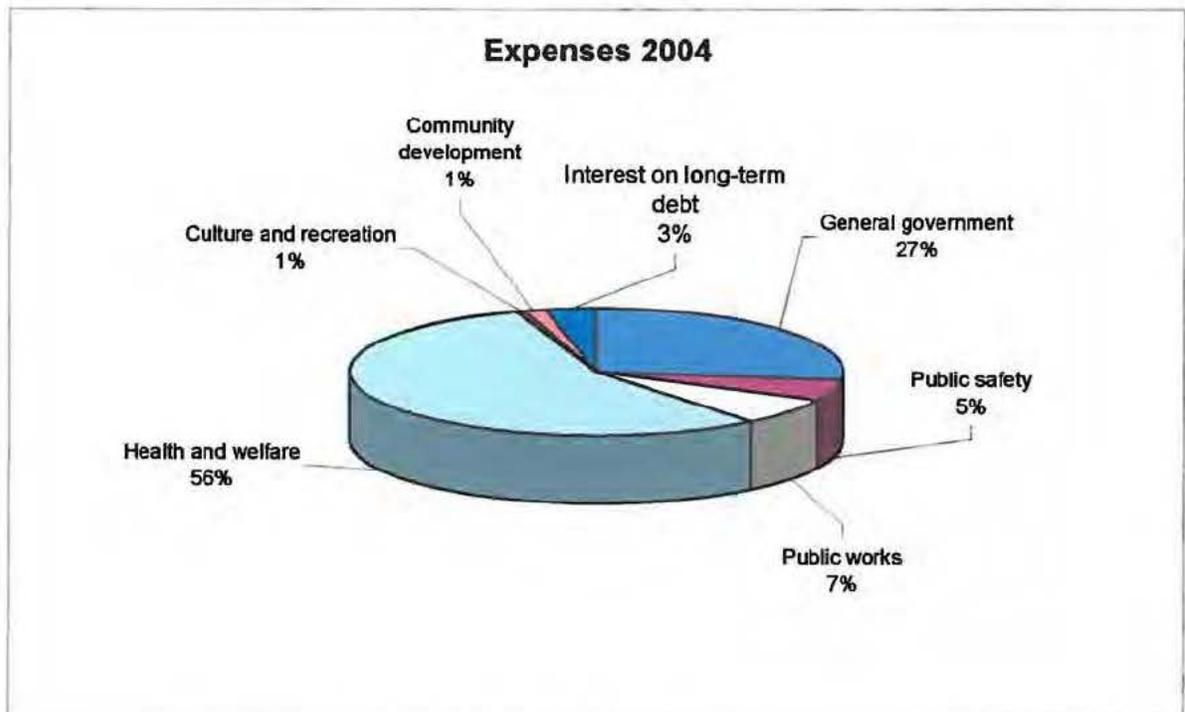
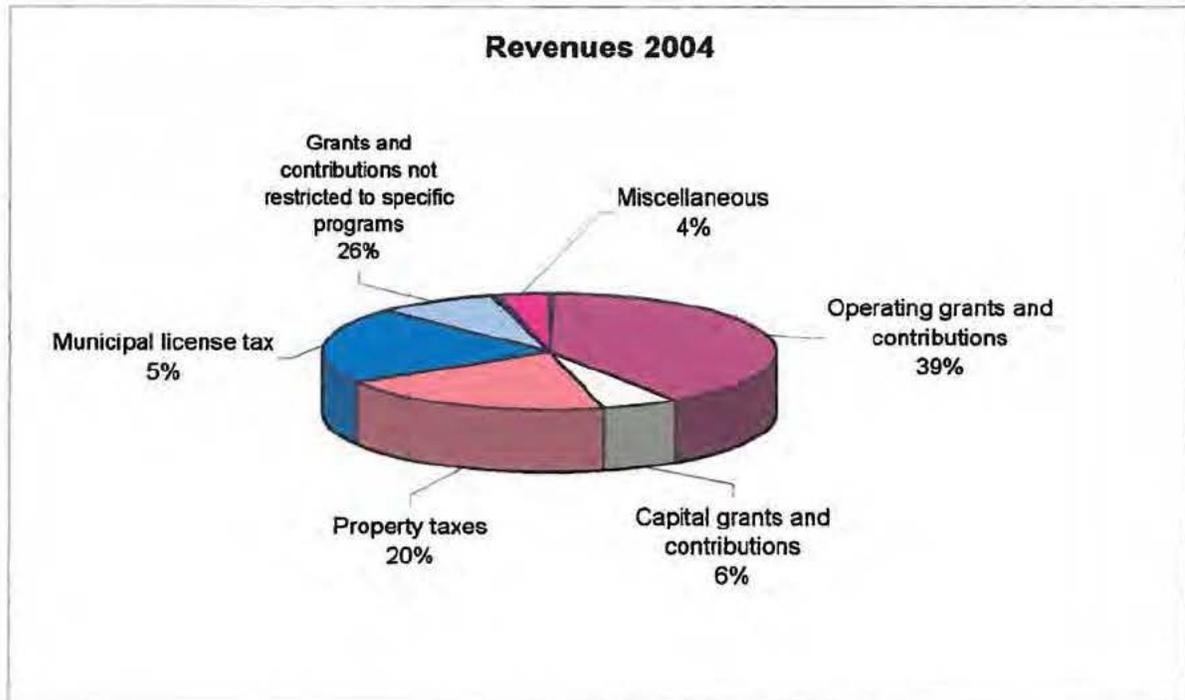
Condensed Statement of Activities	2004	2003	Change	%
Program revenues:				
Charges for services	\$92,925	\$116,543	(\$23,618)	(20%)
Operating grants and contributions	18,062,968	13,384,844	4,678,124	35%
Capital grants and contributions	2,488,257	2,700,140	(211,883)	(8%)
General revenues:				
Property taxes	9,044,204	9,069,713	(25,509)	-
Municipal license tax	9,476,025	9,651,731	(175,706)	(2%)
Grants and contributions not restricted to specific programs	3,885,226	4,341,735	(456,509)	(11%)
Interest and investment earnings	242,764	311,959	(69,195)	(22%)
Miscellaneous	1,594,897	254,352	1,340,545	527%
Total revenues	44,887,266	39,831,017	5,056,249	13%
Expenses:				
General government	8,226,625	9,784,589	(1,557,964)	(16%)
Public safety	1,591,369	1,096,266	495,103	45%
Public works	2,112,173	11,770,584	(9,658,411)	(82%)
Health and welfare	17,038,046	12,668,348	4,369,698	34%
Culture and recreation	171,350	729,402	(558,052)	(77%)
Community development	407,922	541,512	(133,590)	(25%)
Interest on long-term debt	1,013,331	1,005,864	7,467	1%
Education	3,908		3,908	100%
Total expenses	30,564,724	37,596,565	(7,031,841)	(19%)
Change in net assets	14,322,542	2,234,452	12,088,090	541%
Net assets, beginning of year	8,415,199	6,180,747	2,234,452	36%
Net assets, end of year	\$22,737,741	\$8,415,199	\$14,322,542	170%

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA

MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)

YEAR ENDED JUNE 30, 2004

Changes in Net Assets (Continued)



**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA**

MANAGEMENT'S DISCUSSION AND ANALYSIS – (CONTINUED)

YEAR ENDED JUNE 30, 2004

FINANCIAL ANALYSIS OF THE MUNICIPALITY'S INDIVIDUAL FUNDS

As noted earlier, the Municipality uses fund accounting to ensure and demonstrate compliance with finance related legal requirements.

Governmental Funds

The focus of the Municipality's governmental funds is to provide information on near-term inflows, outflows, and balances of spend able resources. Such information is useful in assessing the Municipality's financing requirements. In particular, unreserved fund balance may serve as a useful measure of a government's net resources available for spending at the end of the fiscal year.

As of the end of the current fiscal year, the Municipality's governmental funds reported combined ending fund balances of \$22,016,586, an increase of \$5,935,778 in comparison with the prior year. There are reservations of fund balance amounting to \$20,345,757. This is the fund balance that it is not available for new spending because it has already been committed 1) to liquidate contracts and purchase orders of the prior fiscal year (\$540,244), 2) to pay debt service (\$ 5,070,884), 3) to pay for capital projects (\$11,820,318) and 4) for other purposes (\$ 2,914,311).

Within the governmental funds, it is included the general fund which is the chief operating fund of the Municipality. As of June 30, 2004, the general fund has a fund balance of \$ 2,211,073.

GENERAL FUND BUDGETARY HIGHLIGHTS

Over the course of the year, the Municipality Council revised the Municipality's budget in order to include increases in revenues that were identified during the course of the fiscal year based on current developments that positively affected the Municipality's finances. Increases in budgeted expenditures were also made since the law mandates a balanced budget.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

The Municipality's investment in capital assets as of June 30, 2004, amounts to \$ 37,756,824, net of accumulated depreciation of \$ 2,996,021, leaving a net book value of \$ 34,760,830. This investment in capital assets includes land, buildings, improvements, equipment, infrastructure and construction in progress. Infrastructure

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA**

MANAGEMENT AND DISCUSSION ANALYSIS – (CONTINUED)

YEAR ENDED JUNE 30, 2004

CAPITAL ASSETS AND DEBT ADMINISTRATION- (CONTINUED)

assets are items that are normally immovable and of value only to the state, such as roads, bridges, streets and sidewalks, drainage systems, lighting systems, and similar items.

The total increase in the Municipality's investment in capital assets for the current fiscal year was about 41% in terms of net book value. Depreciation charges for the year totaled \$ 594,126.

The Municipality finances a significant portion of its construction activities through bond issuances. The proceeds from bond issuances designated for construction activities are committed in its entirety for such purposes and cannot be used for any other purposes. As of June 30, 2004, the Municipality has \$11,820,318 of unexpended proceeds mainly from bond issuances that are committed to future construction activities.

Debt Administration

The Puerto Rico Legislature has established a limitation for the issuance of general obligation municipal bonds and notes for the payment of which the good faith, credit and taxing power of each municipality may be pledged. See "Limitations on Ability of Municipalities to Issue General Obligation Debt-The Municipal Bonds" for a general description of such limitations.

The applicable law also requires that in order for a Municipality to be able to issue additional general obligation bonds and notes such Municipality must have sufficient "payment capacity". Act No. 64 provides that a municipality has sufficient "payment capacity" to incur additional general obligation debt if the deposits in such municipality's Redemption Fund and the annual amounts collected with respect to such Municipality's Special Additional Tax (as defined below), as projected by GDB, will be sufficient to service to maturity the Municipality's outstanding general obligation debt and the additional proposed general obligation debt ("Payment Capacity").

The Municipality is required under applicable law to levy the Special Additional Tax in such amounts as shall be required for the payment of its general obligation municipal bonds and notes. In addition, principal of and interest on all general obligation municipal bonds and notes and on all municipal notes issued in anticipation of the issuance of general obligation bonds issued by the Municipality constitute a first lien on the Municipality's Basic Tax revenues. Accordingly, the Municipality's Basic Tax revenues would be available to make debt service payments on general obligation,

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA

MANAGEMENT'S DISCUSSION AND ANALYSIS - (CONTINUED)

YEAR ENDED JUNE 30, 2004

CAPITAL ASSETS AND DEBT ADMINISTRATION- (CONTINUED)

municipal bonds and notes to the extent that the Special Additional Tax levied by the Municipality, together with moneys on deposit in the Municipality's Redemption Fund, are not sufficient to cover such debt service. It has never been necessary to apply Basic Taxes to pay debt service on general obligation debt of the Municipality.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

The Municipality relies primarily on property and municipal taxes as well as federal grants to carry out the governmental activities. Historically, property and municipal taxes have been very predictable with increases of approximately five percent. Federal grant revenues may vary if new grants are available but the revenue also is very predictable.

Those factors were considered when preparing the Municipality's budget for the 2004-2005 fiscal year.

FINANCIAL CONTACT

The Municipality's financial statements are designed to present users (citizens, taxpayer, customers, investors and creditors) with a general overview of the Municipality's finances and to demonstrate the Municipality's accountability. If you have questions about the report or need additional financial information, contact the Municipality's Chief Financial Officer.

Commonwealth of Puerto Rico
Municipality of Guayama
Statement of Net Assets
June 30, 2004

	Governmental Activities
Assets	
Cash and cash equivalents	\$ 14,452,243
Cash with fiscal agent	12,119,232
Accounts receivable:	
Intergovernmental	312,266
Federal grants	3,920,400
Interest	3,258
Other	3,390
Capital assets	
Land, improvements, and construction in progress	19,119,573
Other capital assets, net of depreciation	15,641,230
Total capital assets	<u>34,760,803</u>
Total assets	<u><u>65,571,592</u></u>
Liabilities	
Accounts payable and accrued liabilities	2,441,400
Due to other governmental entities	190,441
Deferred revenues:	
Municipal license tax	5,591,912
Federal grant revenues	570,450
Noncurrent liabilities:	
Due within one year	1,891,192
Due in more than one year	<u>32,148,456</u>
Total liabilities	<u><u>42,833,851</u></u>
Net Assets	
Invested in capital assets, net of related debt	13,351,698
Restricted for:	
Capital projects	11,820,318
Debt service	5,070,884
Federal and state grant funds	2,914,311
Unrestricted (deficit)	<u>(10,419,470)</u>
Total net assets	<u><u>\$ 22,737,741</u></u>

The notes to the financial statements are an integral part of this statement.

Commonwealth of Puerto Rico
Municipality of Guayama
Statement of Activities
For the Year Ended June 30, 2004

Functions/Programs	Expenses	Program Revenues			Net (Expense) Revenue and Changes in Net Assets
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Governmental Activities
General government	\$ 8,226,625	\$ 19,110	\$ 222,656	\$ -	\$ (7,984,859)
Public safety	1,591,369	150	94,016		(1,497,203)
Public works	2,112,173	65,892	358,949	2,418,257	730,925
Health and welfare	17,038,046		13,224,567		(3,813,479)
Culture and recreation	171,350	7,773	554,793	70,000	461,216
Community development	407,922		3,604,079		3,196,157
Education	3,908		3,908		-
Interest on long-term debt	1,013,331				(1,013,331)
Total governmental activities	\$ 30,564,724	\$ 92,925	\$ 18,062,968	\$ 2,488,257	(9,920,574.0)
General revenues:					
Property taxes					9,044,204
Municipal license tax					9,476,025
Grants and contributions not restricted to specific programs					3,885,226
Interest and investment earnings					242,764
Miscellaneous					1,594,897
Total general revenues					24,243,116
Change in net assets					14,322,542
Net assets - beginning as restated					8,415,199
Net assets - ending					\$ 22,737,741

Commonwealth of Puerto Rico
Municipality of Guayama
Balance Sheet
Governmental Funds
June 30, 2004

	General Fund	Special Revenue Fund State & Federal Grants	Capital Projects Fund State & Federal Grants	Debt Service Fund	Total Governmental Funds
Assets					
Cash and cash equivalents	\$ 8,033,279	\$ 1,739,726	\$ 4,679,238	\$ -	\$ 14,452,243
Cash with fiscal agent		575,594	6,531,798	5,011,840	12,119,232
Accounts receivable:					
Intergovernmental			246,953	65,313	312,266
Federal grants		3,471,812	448,588		3,920,400
Interest				3,258	3,258
Other	3,390				3,390
Due from other funds	1,353,392	1,100,259	309,531		2,763,182
Total assets	\$ 9,390,061	\$ 6,887,391	\$ 12,216,108	\$ 5,080,411	\$ 33,573,971
Liabilities and Fund Balances					
Liabilities :					
Accounts payable and accrued liabilities	\$ 617,376	\$ 1,824,024	\$ -	\$ -	\$ 2,441,400
Due to other governmental entities	190,441				190,441
Due to other funds	779,259	1,955,396	19,000	9,527	2,763,182
Deferred revenues:					
Municipal license tax	5,591,912				5,591,912
Federal grant revenues		193,660	376,790		570,450
Total liabilities	7,178,988	3,973,080	395,790	9,527	11,557,385
Fund balances:					
Reserved for:					
Encumbrances	540,244				540,244
Capital projects			11,820,318		11,820,318
Other purposes		2,914,311			2,914,311
Debt service fund				5,070,884	5,070,884
Unreserved:					
Undesigned	1,670,829				1,670,829
Total fund balances	2,211,073	2,914,311	11,820,318	5,070,884	22,016,586
Total liabilities and fund balances	\$ 9,390,061	\$ 6,887,391	\$ 12,216,108	\$ 5,080,411	

Amounts reported for governmental activities in the statement of net assets are different because:

Capital assets used in governmental activities are not financial resources and, therefore, are not reported in the funds	34,760,803
Long-term liabilities are not due and payable in the current period, and therefore, are not reported in the funds	(34,039,648)
Net assets of governmental activities	\$ 22,737,741

Commonwealth of Puerto Rico
Municipality of Guayama
Statement of Revenues, Expenditures and Changes in Fund Balances
Governmental Funds
For the Year Ended June 30, 2004

	General Fund	Special Revenue Fund State & Federal Grants	Capital Projects Fund State & Federal Grants	Debt Service Fund	Total Governmental Funds
Revenues					
Property taxes	\$ 6,672,863	\$ -	\$ -	\$ 2,371,341	\$ 9,044,204
Municipal license taxes	9,476,025				9,476,025
Licenses, permits and other local taxes	1,464,637				1,464,637
Intergovernmental	2,647,856	489,307	954,446		4,091,609
Charges for services	165,128				165,128
Rent of property	147,120				147,120
Fines and forfeitures	150				150
Interest	242,764				242,764
Federal grants		17,040,538	231,871		17,272,409
Miscellaneous	1,289,052	392,183	45		1,681,280
Total revenues	\$ 22,105,595	\$ 17,922,028	\$ 1,186,362	\$ 2,371,341	\$ 43,585,326
Expenditures					
Current:					
General government	7,514,250	664,899			8,179,149
Public safety	1,371,926	221,988			1,593,914
Public works	3,445,617	288,430	4,374,906		8,108,953
Health and welfare	3,986,957	13,255,106			17,242,063
Culture and recreation	821,206	413,945			1,235,151
Community development		3,604,079			3,604,079
Education		3,908			3,908
Debt service:					
Principal				929,000	929,000
Interest				1,013,331	1,013,331
Total expenditures	17,139,956	18,452,355	4,374,906	1,942,331	41,909,548
Excess (deficiency) of revenues over (under) expenditures	4,965,639	(530,327)	(3,188,544)	429,010	1,675,778
Other financing sources (uses)					
Transfers in		1,972,164	2,370,846	30,750	4,373,760
Transfers out	(2,940,427)	(1,433,333)			(4,373,760)
Long-term debt issued			4,260,000		4,260,000
Total other financing sources (uses)	(2,940,427)	538,831	6,630,846	30,750	4,260,000
Net change in fund balances	2,025,212	8,504	3,442,302	459,760	5,935,778
Fund balance, beginning as restated	185,861	2,905,807	8,378,016	4,611,124	16,080,808
Fund balance, ending	\$ 2,211,073	\$ 2,914,311	\$ 11,820,318	\$ 5,070,884	\$ 22,016,586

Commonwealth of Puerto Rico
Municipality of Guayama
Reconciliation of the Statement of Revenues,
Expenditures, and Changes in Fund Balances of
Governmental Funds to the Statement of Activities
For the Year Ended June 30, 2004

Net Change in Fund Balances - Total Governmental Funds **\$ 5,935,778**

Amounts reported for governmental activities in the Statement of Activities are different because:

Governmental Funds report capital outlays as expenditures. However, in the Government-Wide Statement of Activities and Changes in Net Assets, the cost of those assets is allocated over their estimated useful lives as depreciation expense. This is the amount of capital assets recorded in the current period. 9,741,530

Depreciation expense on capital assets is reported in the Government-Wide Statement of Activities and Changes in Net Assets, but they do not require the use of current financial resources. Therefore, depreciation expense is not reported as expenditures in Governmental Funds (594,126)

Some expenses reported in the Statement of Activities do not require the use of current financial resources and, therefore, are not reported as expenditures in Governmental Funds. 177,149

Some revenues reported in the Statement of Activities do not provide current financial resources in Governmental Funds. 1,301,940

Change in landfill accrual 1,091,271

The issuance of long-term debt provides current financial resources to Governmental Funds, while the repayment of principal of long-term debt consumes current financial resources. This is the amount by which debt proceeds exceed debt service principal payments. (3,331,000)

Change in Net Assets of Governmental Activities **\$ 14,322,542**

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA**

NOTES TO BASIC FINANCIAL STATEMENTS

YEAR ENDED JUNE 30, 2004

The **Municipality of Guayama** (the Municipality) was founded on the year 1736. The Municipality's governmental system consists of an executive and legislature body. It is governed by a Mayor and a sixteen-member Municipal Legislature who are elected for a four-year term.

The Municipality provides public safety, public works, culture and recreation, health and welfare, urban development, education, economic development, and other miscellaneous services.

The accounting policies and financial reporting practices of the Municipality conform to accounting principles generally accepted in the United States of America ("GAAP") as applicable to governmental units.

In June 1999, the Governmental Accounting Standards Board (GASB) issued Statement No. 34, "Basic Financial Statements and Management's and Discussion and Analysis for State and Local Governments." This Statement, known as the Reporting Model, provides for the most significant change in financial reporting for state and local governments in over 20 years and affects the way the Municipality prepares and presents financial information. The Statement was adopted as of July 1, 2002. In addition to this Statement, GASB Statement No. 37, "Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments: Omnibus" and GASB Statement No. 38, "Certain Financial Statement Note Disclosures" have been adopted and are reflected in these financial statements.

As part of this Statement, there is a new reporting requirement regarding the capitalization of local government infrastructure (roads, bridges, traffic signals, etc.). This requirement permits an optional four-year delay for implementation to fiscal year 2007. The Municipality has elected to delay the capitalization of infrastructure.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

A. Component Units

In evaluating how to define the Municipality for financial reporting purposes, management has considered all potential component units. The decision to include a potential component unit in the reporting entity was made by applying the provisions of Statement No. 14, The Financial Reporting Entity, of the GASB. The basic, but not the only criterion for including a potential component unit within the reporting entity is if elected officials of a primary government are financially accountable for the entity. Financial accountability exists if the primary governmental appoints a voting majority of the entity's governing body, and if either one of the following conditions exist: the primary government can impose its will on the other entity or the potential exists for the other entity to (1) provide specific financial benefits to or (2) impose specific financial burdens on the primary government. A second criterion used in evaluating potential component units is if the nature and significance of the relationship between the entity and a primary government are such that to exclude the entity from the financial reporting entity would render the financial statements misleading or incomplete. GAAP details two methods of presentation: blending the financial data of the component unit's balances and transactions in a manner similar to the presentation of the Municipality's balances and transactions or discrete presentation of the component unit's financial data in columns separate from the Municipality's balances and transactions.

B. Government-wide and fund financial statements

Financial information of the Municipality is presented in this report as follow:

1. Management's discussion and analysis introduces the basic financial statements and provides an analytical overview of the Municipality's financial activities.
2. The government-wide financial statements (i.e. the statement of net assets and the statement of activities) report information on all the activities of the Municipality and its component unit. Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, if any, which rely to a significant extent on fees and charges for support. Interfund activity has been removed from these statements to minimize the duplicating effect on assets and liabilities within the governmental activities.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment is offset by program revenue. Direct expenses are those that are charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment and 2) grants and contributions that are restricted to meeting the operational or capital requirements of a

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

B. Government-wide and fund financial statements

particular function or segment. Taxes and other items not properly included among program revenues are reported instead as general revenues.

3. Fund financial statements focus on information about the Municipality's major governmental funds. Major individual governmental funds are reported as separate columns in the fund financial statements. The Municipality reports the following major governmental funds:

General Fund- is the accounting entity in which all governmental activity, except that which is required to be accounted for in another fund, is accounted for. Its revenues consist mainly of taxes, licenses and permits, intergovernmental revenue, charges for services and other.

Special Revenue Fund- State and Federal Grants – is the accounting entity in which revenues derived from federal and state grants, is accounted for. The uses and limitations of each special revenue fund are specified by Municipality ordinances or federal and state statutes.

Capital Projects Fund –Local, State and Federal Grants - is the accounting entity in which revenues derived from local funds, state and federal grants or other restricted revenue sources related to capital projects, is accounted for. The uses and limitations of each capital project fund are specified by Municipality ordinances or federal and state statutes.

Debt Service Funds- Debt Service Funds are used to account for the accumulation of resources for and the payment of, general long-term debt principal, interest, and related costs.

4. The notes to the financial statements provide information that is essential to a user's understanding of the basic financial statements.
5. Required supplementary information such as the budgetary comparison schedule-general fund and other types of data required by GASB.
6. Notes to the budgetary comparison schedule-general fund.

C. Financial reporting presentation

The accounts of the Municipality are organized on the basis of funds, each of which is considered a separate accounting entity. The operations of each fund are accounted for with a separate set of self-balancing accounts that comprise its assets, liabilities, fund equity, revenues, and expenditures. Fund types are as follows:

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

C. Financial reporting presentation

General Fund- The General Fund is the general operating fund of the Municipality. It is used to account for all governmental activity, except those required to be accounted for in another fund.

Special Revenue Funds- Special Revenue Funds are used to account for revenues derived from grants or other restricted revenue sources. The uses and limitations of each special revenue fund are specified by Municipality ordinances or federal and state statutes.

Debt Service Funds- Debt Service Funds are used to account for the accumulation of resources for and the payment of, general long-term debt principal, interest, and related costs.

Capital Projects Funds- Capital Project Funds are used to account for financial resources used for the acquisition or construction of major capital facilities.

D. Measurement focus, basis of accounting and financial presentation

Except for budgetary purposes, the basis of accounting used by the Municipality conform to accounting principles generally accepted in the United States of America ("GAAP") as applicable to governmental units. The accounting and financial reporting treatment applied to a fund is determined by its measurement focus.

The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property taxes are recognized as revenues in the year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

The Municipality has elected not to apply all Statements and Interpretations issued by the Financial Accounting Standard Board after November 30, 1989, in accordance with GASB Statement No.20.

Governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the government

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

D. Measurement focus, basis of accounting and financial presentation

considers revenues to be available if they are collected within the current period or soon enough thereafter. Expenditures are recorded when the related fund liability is incurred, except for principal and interest on general long-term debt, claims and judgments, and compensated absences, which are recognized as expenditures when payment is due. General capital asset acquisitions are reported as expenditure in governmental funds. Proceeds from issuance of general long-term debt reported as other financing sources.

Property taxes, franchise taxes, licenses, and interest associated with the current fiscal period are all considered to be susceptible to accrual and so have been recognized as revenues of the current fiscal period. All other revenue items are considered to be measurable and available only when the government receives cash.

Private-sector standards of accounting and financial reporting issue prior to December 1, 1989, generally are followed in the government-wide financial statements to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board. Governments also have the option of following subsequent private-sector guidance for their business-type activities and enterprise funds, subject to this same limitation. The Municipality has elected not to follow subsequent private-sector guidance.

Amounts reported as program revenues include 1) charges to customers or applicants for goods, services, or privileges provided, 2) operating grants, and contributions, and 3) capital grants and contributions, including special assessments, if any. Internally dedicated resources are reported as general revenues rather than as program revenues. Likewise, general revenues include all taxes.

When both restricted and unrestricted resources are available for use, it is the government's policy to use restricted resources first, then unrestricted resources, as they are needed.

The preparation of the financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

E. Assets, liabilities and net assets

- 1. Cash, cash equivalents, and cash with fiscal agent-** The Municipality's cash and cash equivalents are considered to be cash on hand, demand deposits, and short-term investments with original maturities of three months or less from the date of acquisition.

Cash with fiscal agent in the debt services fund represents special additional property tax collections retained by the Commonwealth of Puerto Rico and restricted for the payment of the Municipality's debt service, as established by law.

- 2. Receivables and payables-** Activity between funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as either "due to/from other funds" (i.e., the current portion of interfund loans) or "advances to/from other funds" (i.e., the non-current portion of interfund loans). All other outstanding balances between funds are reported as "due to/from other funds."

Advances between funds, as reported in the fund financial statements, if any, are offset by a fund balance reserve account in applicable governmental funds to indicate that they are not available for appropriation and are not expendable available financial resources.

Receivables are stated net of estimated allowances for uncollectible accounts, which are determined, based upon past collection experience and current economic conditions. Intergovernmental receivables in the general fund represent mostly contributions from the Puerto Rico Electric Power Authority, which contribute a specific percentage of their revenues as payment in lieu of taxes. Intergovernmental receivable in the special revenue fund represent amounts owed to the Municipality for reimbursement of expenditures incurred pursuant to federally funded programs and the amount in the debt service fund represent the distribution of property tax collected by the Municipal Revenue Collection Center (CRIM), which is restricted for the debt service.

- 3. Inventories-** Inventories in the general fund is recorded as expenditure and, consequently, the inventory is not recorded in the statement of net assets.
- 4. Capital assets-** Capital assets, which include property, equipment and infrastructure assets (e.g., roads, bridges, sidewalks and similar items), are reported in the governmental activities column in the governmental-wide financial statements. The Municipality defines capital asset as assets with an initial, individual cost of more than \$25 and an estimated useful life in excess of one year. Such assets are

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

E. Assets, liabilities and net assets

reported at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair market value at the date of donation.

The cost of normal maintenance and repairs that do not add to the value of the asset or materially extend assets lives are not capitalized.

Major outlays for capital assets and improvements are capitalized as projects are constructed.

Capital assets of the Municipality, as well as the component unit, are depreciated using the straight-line method over the following estimated useful lives:

Description	Useful Life	Capitalization threshold
Buildings and site improvements	40 years	\$ 1
Infrastructure	40 years	\$ 1
Works of art	10 years	\$ 1
Vehicles	5 years	\$ 1
Furniture and fixtures	5 years	\$ 25
Machinery and equipment	3 to 5 years	\$ 25

- 5. Long-term obligations-** The liabilities reported in the government-wide financial statements included general and special obligation bonds, bank and long-term notes, other long-term liabilities, such as vacation, sick leave, litigation, long-term liabilities to other governmental entities and landfill closure and post closure care costs.

In the fund financial statements, governmental fund types recognize bond issuances cost, during the current period. The face amount of debt issued is reported as other financing sources, while bond issuance costs, whether or not withheld from the actual debt proceeds received, are reported as expenditures in the general fund.

- 6. Compensated absences-** Employees accumulate vacation leave at a rate of 2.5 days per month up to a maximum of 60 days. Unpaid vacation time accumulated is fully vested to the employees from the first day of work. All vacation pay is accrued when incurred in the government-wide financial statements.

Employees accumulate sick leave at a rate of 1.5 days per month up to a maximum of 90 days. Upon retirement, an employee receives compensation for all accumulated and unpaid sick leave at the current rate, if the employee has at least 10 years of service with the Municipality.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

E. Assets, liabilities and net assets

7. **Claims and judgments-** The estimated amount of the liability for claims and judgments, which is due on demand, such as from adjudicated or settled claims, is recorded in the general fund.
8. **Reservation of fund balance-** Reservations of fund balance in the fund financial statements, represent portions of fund balances that are legally segregated for specific future use or are not appropriated for expenditure. The Municipality has the following reservations of fund balance:
 - a. *Capital Projects-* Represent the reservation of amounts to be used for future expenditures for capital projects under contracts and other commitments. These committed amounts generally will become liabilities in future periods as the projects are completed.
 - b. *Encumbrances-* Represent future expenditures under purchase orders, contracts and other commitments. These committed amounts generally will become liabilities in future periods as the goods or services are received.
 - c. *Debt Service Fund-* Represents net assets available to finance future debt service payments.
 - d. *Other Purposes-* Represents net assets available for specific use and/or legally segregated for other specific future use.
9. **Interfund and intra-entity transactions-** The Municipality has the following types of transactions among funds:
 - a. *Operating Transfers-* Legally required transfers that are reported when incurred as "Operating transfer-in" by the recipient fund and as "Operating transfers-out" by the disbursing fund.
 - b. *Intra-Entity Transactions-* Transfers between the funds of the primary government are reported as interfund transfers with receivables and payables presented as amounts due to and due from other funds.
10. **Risk financing-** The Municipality carries commercial insurance to cover casualty, theft, tort claims and other losses. Insurance policies are negotiated by the Puerto Rico Treasury Department and costs are allocated among all the Municipalities of Puerto Rico. Cost of insurance allocated to the Municipality and deducted from the

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

E. Assets, liabilities and net assets

gross property tax collections by the CRIM for the year ended June 30, 2004 amounted to approximately \$ 353,000. The current insurance policies have not been cancelled or terminated. The CRIM also deducted approximately \$463,000 for workers compensation insurance covering all municipal employees.

11. Reconciliation of Government-Wide and Fund Financial Statements- The governmental fund balance sheet includes reconciliation between fund balance-total governmental funds and net assets-governmental activities as reported in the government-wide statement of net assets. The two elements of that reconciliation explains that "long term liabilities, including compensated absences, bonds and notes payable, are not due and payable in the current period and therefore are not reported in the funds.", and that "capital assets used in governmental activities are not financial resources and, therefore, are not reported in the funds. The detail of this reconciliation is as follows:

		<u>Total Net Assets - Governmental Activities</u>
<u>Net assets invested in capital assets, net of related debt</u>		
Capital assets, net of depreciation	\$ 34,760,803	
Deduct:		
Bonds Payable	<u>(21,409,105)</u>	13,351,698
<u>Net assets restricted for capital projects</u>		
Fund balance restricted for capital projects		11,820,318
<u>Net assets restricted for debt service</u>		
Fund balance restricted for debt service		5,070,884
<u>Net assets restricted for other purposes</u>		
Fund balance restricted for other purposes		2,914,311
<u>Net assets unrestricted (deficit)</u>		
General fund - total fund balance:	\$ 2,211,073	
Deduct:		
Compensated absences	(2,373,723)	
Landfill obligation	(6,784,100)	
Advances from CRIM	(292,497)	
Other Liabilities	<u>(3,180,223)</u>	<u>(10,419,470)</u>
Total net assets - governmental activities		<u>\$ 22,737,741</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

2. DEPOSITS

Under Puerto Rico statutes public funds deposited in commercial banks must be fully collateralized for the amount deposited in excess of federal depository insurance. All securities pledged as collateral are held by the Secretary of the Treasury of Puerto Rico. In addition, the Municipality maintains deposits with the Government Development Bank for Puerto Rico (GDB).

The Municipality's bank balances in commercial banks of approximately \$ 8,000,000 in the general fund were fully collateralized at June 30, 2004. In the other major governmental funds there were deposits with commercial banks of approximately \$ 6,400,000 that were fully collateralized.

The deposits at GDB of approximately \$ 7,100,000 that are restricted principally for capital projects, and the \$ 5,011,840 in the debt service fund are unsecured and uncollateralized, as no collateral is required to be carried by governmental banks.

3. RECEIVABLES

- a. **Municipal License Tax**- The Municipality imposes a municipal license tax on all businesses that operate within the Municipality, which are not totally or partially exempt from the tax pursuant to the Industrial Incentives Acts of the Commonwealth of Puerto Rico. This is a self-assessed tax based on the business volume in gross sales as shown in the tax return that is due on April 15 of each year. Entities with sales volume of \$ 1,000,000 or more must include audited financial statements together with the tax return. During the fiscal year ended June 30, 2004, the tax rates were as follows:

- Financial business- 1.50% of gross revenues
- Other organizations within municipal area - 0.30% of gross revenues
- Other organizations 0.50% of gross revenues

This tax is due in two equal installments on July 1 and January 1 of each fiscal year. A discount of 5% is allowed when full payment is made on or before April 15. Municipal license tax receivable represents filed municipal license tax returns that were uncollected as of June 30, 2004, net of allowance for uncollectibles. Municipal license taxes collected prior to June 30 but pertaining to the next fiscal year are recorded as deferred revenues.

- b. **Intergovernmental Receivables**- Intergovernmental receivables in the Capital Projects Fund consist of amounts due from the Governmental Development Bank of Puerto Rico.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

3. RECEIVABLES (CONTINUED)

c. *Federal Grants*- Federal Grants receivable in the Special Revenue and Capital Projects Funds mainly consist in expenditures incurred not yet reimbursed by the CDBG and FEMA Programs.

4. INTERFUND TRANSACTIONS

Interfund receivables and payables at June 30, 2004 are summarized as follows:

a. Due from/to other fund:

<u>Receivable Fund</u>	<u>Payable Fund</u>	<u>Amount</u>
General	Special Revenue Fund	\$ 1,324,865
	Capital Projects Fund	19,000
	Debt Service Fund	9,527
Special Revenue	Special Revenue Fund (02)	16,000
	Special Revenue Fund (07)	305,000
	General Fund	779,259
Capital Projects	Special Revenue Fund	<u>309,531</u>
Total		<u>\$ 2,763,182</u>

b. Transfer in/out to other fund

Following is a summary of interfund transfers for the year:

<u>Transfer out</u>	<u>Transfer in</u>	<u>Purpose</u>	<u>Amount</u>
General Fund	Capital Projects Fund	Transfer of funds for Capital Outlays	\$ 937,513
Special Revenue Fund	Capital Projects Fund	Transfer of funds for Capital Outlays	1,433,333
General Fund	Special Revenue Fund	Various	1,972,164
Debt Service Fund	General Fund	Debt Retirement	<u>30,750</u>
Total			<u>\$ 4,373,760</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

5. CAPITAL ASSETS:

Capital assets; those with an estimated useful life of one year or more from the time of acquisition by the Municipality and a cost of \$25 or more, are primarily funded through the issuance of long-term bonds and loans. A summary of capital assets and changes occurring in 2004, including those changes pursuant to the implementation of GASB Statement No. 34, follows. Land and construction in progress are not subject to depreciation:

Governmental Activities:	Balance July 1, 2003	Additions	Retirements	Balance June 30, 2004
Capital asset, not being depreciated:				
Construction in Progress	\$ 4,414,663	\$6,110,901	(343,877)	\$10,181,687
Land	7,702,324	1,235,562		8,937,886
Total capital assets not being depreciated	12,116,987	7,346,463	(343,877)	19,119,573
Capital assets, being depreciated:				
Buildings and building improvements	12,433,806	2,668,482		15,102,288
Infrastructure and infrastructure improvements	253,135	901,554		1,154,689
Equipment	675,190	67,046		1,896,925
Computers	131,427	16,188		147,615
Furnishing	790,794	10,237		948,646
Vehicles	655,892	33,500		689,392
Total capital assets being depreciated	\$14,940,244	\$3,697,007		\$18,637,251

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA**

NOTES TO GENERAL PURPOSE FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

5. CAPITAL ASSETS (CONTINUED):

Less accumulated depreciation for:

Buildings and building improvements	(\$560,301)	(\$333,384)	(\$893,685)
Infrastructure and infrastructure improvements	(7,143)	(41,649)	(48,792)
Equipment	(509,500)	(72,935)	(582,435)
Computers	(111,380)	(13,992)	(125,372)
Furnishing	(599,540)	(115,074)	(714,614)
Vehicles	(614,031)	(17,092)	(631,123)
	<u>(2,401,895)</u>	<u>(594,126)</u>	<u>(2,996,021)</u>
Total accumulated depreciation			
Total capital assets being depreciated, net	<u>12,538,349</u>	<u>3,102,881</u>	<u>15,641,230</u>
Governmental activities capital assets, net	<u>\$24,655,336</u>	<u>\$10,449,344</u>	<u>(\$343,877)</u> <u>\$34,760,803</u>

Depreciation expense was charged to functions/programs of the Municipality as follows:

Governmental activities:

General government	\$444,655
Public safety	8,708
Health and Welfare	11,328
Public works	23,670
Culture and recreation	99,113
Community development	<u>6,652</u>
Total depreciation expense-governmental activities	<u>\$594,126</u>

6. PROPERTY TAXES

The personal property tax is self assessed by the taxpayer on a return which is to be filed by May 15 of each year with the CRIM, a governmental entity created by the government of Puerto Rico as part of the Municipal Governmental Autonomous Law of August 1991. Real property tax is assessed by the CRIM on each piece of real estate and on each building.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

6. PROPERTY TAXES (CONTINUED):

The assessment is made as of January 1 of each year and is based on current values for personal property and on estimated values as of 1957 for real property tax. The tax on personal property must be paid in full together with the return by May 15. The tax on real property may be paid in two installments by July 1 and January 1. The CRIM is responsible for the billing and collections of real and personal property taxes on behalf of all the municipalities of Puerto Rico. Prior to the beginning of each fiscal year, the CRIM informs the Municipality of the estimated amount of property tax expected to be collect for the ensuing fiscal year. Throughout the year, the CRIM advances funds to the Municipality based on the initial estimated collections. The CRIM is required by law to prepare a settlement statement on a fiscal year basis, whereby a comparison is made between the amounts advanced to the Municipality and amounts actually collected from taxpayers. This settlement has to be completed on a preliminary basis not later than three months after fiscal year-end, and a final settlement made not later than six months after year-end. If the CRIM remits to the Municipality property tax advances, which are less than the tax actually collected, a receivable from the CRIM is recorded at June 30.

Residential real property occupied by its owner is exempt by law from the payment of property taxes on the first \$15,000 of the assessed value. For such exempted amounts, the

Puerto Rico Treasury Department assumes payment of the basic tax to the Municipalities, except for property assessed at less than \$ 3,500 for which no payment is made. As part of the Municipal Autonomous Law of 1991, the exempt amount to be paid by the Puerto Rico Treasury department to the Municipalities was frozen as of January 1, 1992. In addition, the law grants a tax exemption from the payment of personal property taxes of up to \$50,000 of the assessed value to retailers having annual net sales of less than \$150,000.

The annual tax rate is 8.33% for real property and 6.33% for personal property of which 1.03% of both tax rates are for the redemption of public debt issued by the Commonwealth of Puerto Rico. The remaining percentage is distributed as follows: (a) 5.8% and 3.8%, respectively, represents the Municipality's basic property tax rate which is appropriated for basics and accounted for in the general fund. A portion of such amount is deposited in an equalization fund together with a percentage of the net revenues of the Puerto Rico electronic lottery and a subsidy from the Commonwealth of Puerto Rico. From such fund, a distribution is made to all municipalities; (b) 1.50% represents the ad valorem tax restricted for debt service and accounted for in the debt service fund. The Commonwealth also contributes an annual tax rate of 0.2% of the property tax collected and such amount is accounted for similar to item (a) above.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

7. DUE TO OTHER GOVERNMENTAL ENTITIES:

The amounts due to other governmental entities in the General Fund include the following:

General Services Administration	\$ 10,101
Treasury Department	20,588
Puerto Rico Aqueduct and Sewer Authority	20,696
State Insurance Fund	132,893
Other	<u>6,163</u>
Total	<u>\$ 190,441</u>

The Municipality reached agreements with the Department of Treasury, the Department of Labor and the Municipal Revenue Collection Center for the payment of debts on a long-term basis. These liabilities are presented in the Statement of Net Assets as non-current liabilities.

8. DEFERRED REVENUES

- a. **Municipal License Tax-** The deferred revenues of approximately \$5,591,912 in the general fund relates to municipal license tax collected in fiscal year 2003-04 that will be earned in fiscal year 2004-05.
- b. **Federal Government-** The deferred revenues presented in major governmental funds represents the portion of federal grants received for which qualifying expenditures have not been incurred. Deferred revenues from the federal government are as follows:

Program Description	
Section 8 Housing Choice Vouchers	\$ 159,604
UDAG	375,010
Other	<u>35,836</u>
Total	<u>\$ 570,450</u>

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

9. LONG-TERM LIABILITIES

Long-term liability activity for the year ended June 30, 2004, was as follows:

	Beginning Balance	Borrowings or Additions	Payments or Deductions	Ending Balance	Due Within One Year
Bonds Payable	\$18,078,105	\$4,260,000	(\$929,000)	\$21,409,105	\$1,052,000
Advances from CRIM	1,343,879	174,207	(87,470)	1,430,616	261,677
Compensated Absences	2,220,094	153,629		2,373,723	160,000
Landfill obligation	7,875,371		(1,091,271)	6,784,100	
Due to other governmental entities	<u>2,459,619</u>		<u>(417,515)</u>	<u>2,042,104</u>	<u>417,515</u>
Total	<u>\$31,977,068</u>	<u>\$4,587,836</u>	<u>(\$2,525,256)</u>	<u>\$34,039,648</u>	<u>\$1,891,192</u>

- a. Legal debt margin-** The Municipality is subject to a legal debt margin requirement, which is equal to 10% of the total assessment if property located within the Municipality plus balance of the ad valorem taxes in the debt service fund, for bonds payable to be repaid with the proceeds of property taxes restricted for debt service. In addition, before any new bonds are issued, the revenues if the debt service fund should be sufficient to cover the projected debt service requirement. Long-term debt, except for the bonds payable, is paid with unrestricted funds.
- b. Bonds payable-** The Municipality issues general and special obligation bonds to provide funds for the construction of major capital facilities. During the current year, the Municipality issued bonds for approximately \$4,260,000. Bonds payable outstanding at June 30, 2004 are as follows:

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

9. LONG-TERM LIABILITIES (CONTINUED):

Type of bonds	Maturity date	Original amount	Range of Interest rates	Balance at June 30, 2004
1995 Series	7-1-09	4,765,000	6.10% to 7.70%	2,570,000
1996 Series	7-1-20	5,105,000	4.70% to 6.60%	4,430,000
1996 Series	1-1-20	27,000	4.50%	20,000
1996 Series	1-1-20	550,000	4.50%	489,105
1997 Series	7-1-16	400,000	5.00% to 8.00%	300,000
1998 Series	7-1-12	825,000	6.00% to 7.50%	630,000
2000 Series	7-1-24	4,590,000	7.00% to 7.50%	4,285,000
2000 Series	7-1-04	425,000	7.00% to 8.00%	100,000
2000 Series	7-1-17	3,840,000	7.00% to 7.50%	3,355,000
2003 Series	7-1-09	355,000	5.00% to 6.50%	315,000
2003 Series	7-1-27	705,000	5.00% to 6.50%	695,000
2003 Series	7-1-27	2,450,000	5.00% to 6.50%	2,410,000
2004 Series	7-1-23	1,810,000	2.36% to 6.00%	<u>1,810,000</u>

Total general obligation bonds \$21,409,105

These bonds are payable from the ad valorem property tax of 1.50% which is restricted for debt service and retained by the Government Development Bank for Puerto Rico for such purposes.

Annual debt service requirements to maturity for bonds payable are as follows:

Year Ending June 30,	Principal	Interest
2005	1,052,000	1,083,357
2006	1,023,000	1,135,106
2007	1,109,000	1,075,156
2008	1,190,000	1,008,909
2009	1,266,000	936,352
2010-2014	5,097,000	3,732,496
2015-2019	5,430,000	2,316,865
2020-2024	3,967,105	895,733
2025-2029	1,275,000	133,160
Total	<u>\$21,409,105</u>	<u>\$12,317,134</u>

c. **Advances from CRIM-** This amount represents the balance owed to CRIM at June 30, 2004 will be repaid mainly through a financing obtained by the CRIM with GDB.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

9. LONG-TERM LIABILITIES (CONTINUED):

- d. Compensated absences-** The government-wide statement of net assets includes approximately \$ 2,400,000 of accrued vacation and sick leave benefits, representing the Municipality's commitment to fund such costs from future operations.
- e. Landfill obligation-** State and federal laws and regulations require the Municipality to place a final cover on its landfill site, when it stopped accepting waste, and perform certain maintenance and monitoring functions at the site for 30 years after closure. In accordance with Statement No. 18 of the GASB, "Accounting for Municipal Solid Waste Landfill Closure and Post-closure Care Costs", the Municipality has performed a study of the activities that need to be implemented at the Municipality's landfill to guarantee the maximum yield of available space and to comply with applicable state and federal regulations. Based on this study, the Municipality has recognized \$6,784,100 as the Municipality's estimated current cost for landfill closure and post-closure costs as of June 30, 2004. The annual estimate of post closure costs has been assessed approximately to be \$ 47,000 for a period of approximately 30 years. Actual costs may be different due to inflation, changes in technology, or changes in laws and regulations. The balance of closure and post-closure costs are reported in the government-wide statement of net assets.

10. PENSION PLAN

The Employee's Retirement System of the Commonwealth and its Instrumentalities (the Retirement System) is a cost-sharing multiple defined benefit pension plans sponsored by, and reported as a component unit of the Commonwealth of Puerto Rico. All regular employees of the Municipality under 55 years of age at the date of employment become members of the Retirement System as a condition to their employment.

The Retirement System provides retirement, death and disability benefits pursuant to legislation enacted by the Commonwealth's legislature. Disability retirement benefits are available to members for occupational and non-occupational disabilities. Retirement benefits depend upon age at retirement and the number of years of creditable service. Benefits vest after ten years of plan participation.

Members who have attained 55 years of age and have completed at least 25 years of creditable service or members who have attained 58 years of age and have completed ten years of creditable service are entitle to an annual benefit payable monthly for life.

The amount of the annuity shall be one and one-half percent of the average compensation, as defined, multiplied by the number of years of creditable service up to twenty years, plus

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

10. PENSION PLAN (CONTINUED)

two percent of the average compensation, as defined, multiplied by the number of years of creditable service in excess of 20 years. In no case will the annuity be less than \$200 per month.

Participants who have completed at least 30 years of creditable service are entitled to receive the Merit Annuity. Participants who have not attained 55 years of age will receive 65 percent of the average compensation, as defined; otherwise they will receive 75 percent of the average compensation, as defined. No benefits are payable if the participant receives a refund of his/her accumulated contributions.

Commonwealth legislation requires employees to contribute 5.775% for the first \$550 of their monthly gross salary and 8.275% for the excess over \$550 of monthly gross salary. The Municipality is required by the same statute to contribute 9.275% of the participant's gross salary. Total Municipality contributions to the above-mentioned plans during the year ended June 30, 2004 recorded as pension expenditures were approximately **\$ 454,383**. This amount represents 100% of the required contribution for the fiscal year ended June 30, 2004.

On September 24, 1999, an amendment to Act No. 447 of May 15, 1951, which created the Retirement System, was enacted with the purpose of establishing a new pension program (System 2000). Employee's participation in the current system as of December 31, 1999, may elect to stay in the defined benefit plan or transfer to the new program. Persons joining the Municipality on or after January 1, 2000, will only be allowed to become members of System 2000. System 2000 will reduce the retirement age from 65 years to 60 for those employees who joined the current plan on or after April 1, 1990.

System 2000 is a hybrid defined contribution plan, also known as a cash balance plan. Under this new plan, there will be a pool of pension assets, which will be invested by ERS together with those of the current defined benefit plan. The Commonwealth of Puerto Rico will not guarantee benefits at retirement age. The annuity will be based on a formula which assumes that each year the employee's contribution (with a minimum of 8.275% to the employee's salary up to a maximum of 10%) will be invested in an account which will either: (1) earn a fixed rate based on the two-year Constant Maturity Treasury Note or, (2) earn a rate equal to 75% of the return of the ERS's investment portfolio (net of management fees), or (3) earn a combination of both alternatives. Participants will receive periodic account statements similar to those of defined contribution plans showing their accrued balances. Disability pensions will not be granted under System 2000. The employer's contribution (9.275% of the employee's salary) will be used to fund the current plan

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA**

NOTES TO BASIC FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

10. PENSION PLAN (CONTINUED)

Additional information on the Retirement System is provide in its financial statements for the year ended June 30, 2004, a copy of which can be obtained from the Retirement System, Minillas Station, P.O. Box 42004, San Juan, PR 00940

11. COMMITMENTS AND CONTINGENCIES

A. Federal grants:

The Municipality participates in a number of Federal Financial Assistance Programs. Although the Municipality's grant programs have been audited in accordance with the provisions of the Single Audit Act of 1996, through June 30, 2004, these programs are still subject to financial and compliance audits by the granting agencies and the resolution of previously identified questioned costs. The amount, if any, of expenditures which may be disallowed by the granting agencies cannot be determined at this time, although the Municipality expects such amounts, if any, not to be material.

B. Claims and lawsuits:

The Municipality is a defendant in several legal proceedings that arise in the ordinary course of the Municipality's activities. Certain of these claims are covered by insurance. The administration believes that the ultimate liability, if any, would not be significant. As a result, the accompanying general-purpose financial statements do not include adjustments, if any, that could result from the resolution of these legal proceedings.

12. BEGINNING FUND BALANCES RESTATEMENT:

The beginning fund balances of the Debt Service Fund have been restated by \$ 59,044 to properly present the previously reported fund balance as of June 30, 2003.

**COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA**

BUDGETARY COMPARISON SCHEDULE- GENERAL FUND

YEAR ENDED JUNE 30, 2004

	<u>Budgeted Amounts</u>		<u>Actual Amounts</u> (Budgetary Basis)	<u>Variance with</u> <u>Final Budget</u>
	<u>Original</u>	<u>Final</u>	(See Note 1)	<u>Positive</u> <u>(Negative)</u>
Revenues and other financing sources:				
Property taxes	\$6,551,175	\$ 6,672,863	\$ 6,672,863	\$ -
Municipal license tax	7,905,000	8,752,303	9,476,025	723,722
Licenses, permits and other local taxes	808,500	1,404,728	1,464,637	59,909
Intergovernmental	2,741,270	2,833,574	2,647,856	(185,718)
Rent of property	25,000	152,811	147,120	(5,691)
Fines and forfeitures	1,000	150	150	-
Interest	100,000	179,973	242,764	62,791
Miscellaneous	230,000	935,817	1,289,052	353,235
Charge for Services	<u>173,500</u>	<u>20,005</u>	<u>165,128</u>	<u>145,123</u>
Total revenues and other financing sources	<u>18,535,445</u>	<u>20,952,224</u>	<u>22,105,595</u>	<u>1,153,371</u>
Expenditures and other financing uses:				
Current:				
General government	7,070,328	8,145,172	7,522,297	622,875
Public safety	1,841,853	1,497,403	1,373,088	124,315
Public works	3,951,657	3,935,483	3,452,323	483,160
Health and welfare	4,437,565	4,186,400	3,989,040	197,360
Culture and recreation	1,234,042	910,053	821,935	88,118
Transfer to other fund	-	<u>2,277,713</u>	<u>2,277,713</u>	-
Total expenditures and other financing uses	<u>18,535,445</u>	<u>20,952,224</u>	<u>19,436,396</u>	<u>1,515,828</u>
Excess of revenues and other financing sources over (under) expenditures and other financing uses			<u>\$ 2,669,199</u>	<u>\$2,669,199</u>
Explanation of Differences:				
Sources/inflows of resources:				
Actual amounts (budgetary basis)"available for appropriation" from the budgetary comparison schedule				\$ 22,105,595
Differences-budget to GAAP				-
Budgeted carryover				-
Total revenues as reported on the statement of revenues, expenditures, and changes in fund balances				<u>\$ 22,105,595</u>
Uses/outflows of resources:				
Actual amounts (budgetary basis)"total charges to appropriations" from the budgetary comparison schedule				\$ 19,436,396
Differences-budget to GAAP:				
Transfer to other funds are outflows of budgetary resources but are not expenditures for financial reporting purpose				662,714
Nonbudgeted expenditures				
Prior year encumbrances recorded as current year expenditures for GAAP basis				521,517
Current year encumbrances recorded as expenditures for budgetary purposes				<u>(540,244)</u>
Total expenditures as reported on the statement of revenues, expenditures, and changes in fund balances				<u>\$ 20,080,383</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA

NOTES OF BUDGETARY COMPARISON SCHEDULE- GENERAL FUND

YEAR ENDED JUNE 30, 2004

1. STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

a. Budgetary Control

The Municipality's annual budget is prepared on the budgetary basis of accounting, which is not in accordance with GAAP, and represents departmental appropriations recommended by the Mayor and approved by the Municipal Legislature prior to the beginning of the fiscal year. Amendments to the budget require the approval of the Municipal Legislature. Transfers of appropriations within the budget, known as Mayor's Resolutions, do not require the approval of the Municipal Legislature.

The Municipality prepares its annual budget including the operations of the general fund.

For budgetary purposes, encumbrance accounting is used. The encumbrances (i.e., purchase orders, contracts) are considered expenditures when incurred. For GAAP reporting purposes, encumbrances outstanding at year-end are reported as reservations of fund balances and do not constitute expenditures or liabilities because the commitments will be honored during the subsequent year.

The unencumbered balance of any appropriation at the end of the fiscal year will lapse at the end of such fiscal year. Other appropriations, mainly capital project appropriations, are continuing accounts for which the Municipal Legislature has authorized that an unspent balance from the prior year be carried forward and made available for current spending.

The annual budget as presented in the Budgetary Comparison Schedule-General Fund is the budget ordinance at June 30, 2004 representing the original budget. There were no supplemental appropriations for the year ended June 30, 2004.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

YEAR ENDED JUNE 30, 2004

Federal Grantor/Pass-through Grantor/Program or Cluster Title	Federal CFDA Number	Pass-through Entity Identifying Number	Federal Expenditures
U.S. DEPARTMENT OF AGRICULTURE			
Pass-through Commonwealth of Puerto Rico Department of Education:			
Child Care and Adult Food Program	10.558		902,433
Total U.S. Department of Agriculture			<u>902,433</u>
U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT:			
Direct Programs:			
Section 8 - Housing Choice Voucher	14.871		956,528
Pass-through Office of the Commissioner of Municipal Affairs:			
Community Development Block Grant			
State Block Grant Program	14.228	B-93-FD-26	
State Block Grant Program	14.228	B-94-FD-26	
State Block Grant Program	14.228	B-95-FD-26	
State Block Grant Program	14.228	B-96-FD-26	
State Block Grant Program	14.228	B-97-FD-26	
State Block Grant Program	14.228	B-98-FD-26	
State Block Grant Program	14.228	B-99-FD-26	
State Block Grant Program	14.228	B-00-FD-26	
State Block Grant Program	14.228	B-01-FD-26	
State Block Grant Program	14.228	B-02-FD-26	
State Block Grant Program	14.228	B-03-FD-26	
			<u>3,604,079</u>
Total U.S. Department of Housing and Urban Development			<u>4,560,607</u>
U.S. FEDERAL EMERGENCY MANAGEMENT AGENCY:			
Pass-through the Commonwealth of Puerto Rico Governor Authorized Representative (GAR):			
Public Assistance Grants	83.544		208,950

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS - (CONTINUED)

YEAR ENDED JUNE 30, 2004

Federal Grantor/Pass-through Grantor/Program or Cluster Title	Federal CFDA Number	Pass-through Entity Identifying Number	Federal Expenditures
Hazard Mitigation Grant	83.548		231,871
Total U.S. Federal Emergency Management Agency			<u>440,821</u>
U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES			
Pass-through Commonwealth of Puerto Rico			
Administration for Children and Families:			
Head Start	93.600	02-CH-0483-34	11,364,606
Pass-through the Commonwealth of Puerto Rico Department of Education:			
Library Services and Technology Grant	N/A		<u>3,908</u>
Total U.S. Department of Health and Human Services			<u>11,368,514</u>
TOTAL EXPENDITURES OF FEDERAL AWARDS			<u>\$17,272,375</u>

The accompanying notes are an integral part of this schedule.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA

NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

YEAR ENDED JUNE 30, 2004

1. BASIS OF PRESENTATION:

The accompanying Schedule of Expenditures of Federal Awards includes the federal grant activity of the Municipality of Guayama and is presented on the modified accrual basis of accounting. The basis of accounting is the same used to prepare the basic financial statements. The information in this Schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*.

2. RELATIONSHIP TO FEDERAL FINANCIAL REPORTS:

Amounts reported in the accompanying Schedule are included in the Special Revenue and Capital Projects Funds in the Municipality's basic financial statements. The reconciliation between the expenditures in the basic financial statements and the disbursements in the Schedule of Expenditures of Federal Awards is as follows:

Description	Special Revenue	Capital Projects	Total
Per Schedule of Expenditures of Federal Awards	\$17,040,504	\$231,871	\$17,272,375
Non federal programs Expenditures	<u>1,411,851</u>	<u>4,143,035</u>	<u>5,554,886</u>
Total expenditures in the basic financial statements	<u>\$18,452,355</u>	<u>\$4,374,906</u>	<u>\$22,827,261</u>

3. SUBRECIPIENTS:

The Municipality of Guayama provided Federal Awards to sub-recipients as follow:

Program Title	Federal CFDA Number	Amount Provided
<u>Community Development Block Grants-State Block Grants</u>	14.228	<u>\$56,250</u>



López-Vega, CPA, PSC

Certified Public Accountants / Management Advisors

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INDEPENDENT AUDITORS' REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

**To the Honorable Mayor
and the Municipal Legislature
Municipality of Guayama
Guayama, Puerto Rico**

We have audited the general purpose financial statements of the **Municipality of Guayama** as of and for the year ended June 30, 2004, and have issued our report thereon dated December 20, 2004, which was unqualified. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether the **Municipality of Guayama's** basic financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of basic financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the **Municipality of Guayama's** internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the basic financial statements and not to provide assurance on the internal control over financial reporting. However, we noted a matter involving the internal control over financial reporting that, in our judgment, could adversely affect **Municipality of Guayama's** ability to record, process, summarize, and report financial data consistent with the assertions of management in the basic financial statements. The reportable conditions are described in the accompanying schedule of findings and questioned costs items 04-01 and 04-02.

INDEPENDENT AUDITORS' REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER
FINANCIAL REPORTING BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN
ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS (CONTINUED)

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the basic financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose reportable conditions that are also considered to be material weaknesses. However, we believe that none of the reportable conditions described in the accompanying Schedule of Findings and Questioned Costs is a material weakness. We also noted other matters involving the internal control over financial reporting, which we have reported to management of the Municipality of Guayama in a separate letter dated December 20, 2004.

This report is intended for the information of the management and federal awarding agencies and pass-through entities. However, this report is a matter of public record and its distribution is not limited.


LOPEZ-VEGA, CPA, PSC

San Juan, Puerto Rico
December 20, 2004

Stamp No. 2019431 of the Puerto Rico
Society of Certified Public Accountants
was affixed to the record copy of this report.





López-Vega, CPA, PSC

Certified Public Accountants / Management Advisors

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**INDEPENDENT AUDITORS' REPORT
ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO EACH MAJOR PROGRAM AND ON
INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB-CIRCULAR A-133**

**To the Honorable Mayor
and the Municipal Legislature
Municipality of Guayama
Guayama, Puerto Rico**

Compliance

We have audited the compliance of the **Municipality of Guayama** with the types of compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended June 30, 2004. The **Municipality of Guayama's** major federal programs are identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of the **Municipality of Guayama's** management. Our responsibility is to express an opinion on the **Municipality of Guayama's** compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in the *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the **Municipality of Guayama's** compliance with those requirements and performing such other procedures, as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the **Municipality of Guayama's** compliance with those requirements.

In our opinion, the **Municipality of Guayama** complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended June 30, 2004. However, the results of our auditing procedures disclosed instances of noncompliance with those requirements that are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying schedule of findings and questioned costs as items, 04-03 through 04-11.

**INDEPENDENT AUDITORS' REPORT
ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO EACH MAJOR PROGRAM AND ON
INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB-CIRCULAR A-133
(CONTINUED)**

Internal Control Over Compliance

The management of the **Municipality of Guayama** is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered the **Municipality of Guayama's** internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

We noted certain matters involving the internal control over compliance and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over compliance that, in our judgment, could adversely affect the **Municipality of Guayama's** ability to administer a major federal program in accordance with applicable requirements of laws, regulations, contracts and grants. Reportable conditions are described in the accompanying Schedule of Findings and Questioned Costs as items **04-03** through **04-11**.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with applicable requirements of laws, regulations, contracts and grants that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees on the normal course of performing their assigned functions. Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be material weakness. However, of the reportable conditions described above, we consider items **04-04** through **04-06**, **04-09**, and **04-11** to be material weaknesses. We also noted other matters involving the internal control over compliance and certain immaterial instance of noncompliance, which we have reported to management of the **Municipality of Guayama** in a separate letter dated March 5, 2005.



**INDEPENDENT AUDITORS' REPORT
ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO EACH MAJOR PROGRAM AND ON
INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB-CIRCULAR A-133
(CONTINUED)**

This report is intended for the information of the management and federal awarding agencies and pass-through entities. However, this report is a matter of public record and its distribution is not limited.



LOPEZ-VEGA, CPA, PSC

San Juan, Puerto Rico

March 5, 2005

Stamp No. 2019432 of the Puerto Rico
Society of Certified Public Accountants
was affixed to the record copy of this report.



COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

YEAR ENDED JUNE 30, 2004

Section I – Summary of Auditors’ Results

Financial Statements

Type of auditors’ report issued:	Unqualified
Internal control over financial reporting:	
Material weakness identified?	Yes No <input checked="" type="checkbox"/>
Reportable conditions identified not considered to be material weaknesses?	Yes <input checked="" type="checkbox"/> None reported
Noncompliance material to financial statements noted?	Yes No <input checked="" type="checkbox"/>

Federal awards

Internal Control over major programs:	
Material weakness identified?	Yes <input checked="" type="checkbox"/> No
Reportable conditions identified not considered to be material weaknesses?	Yes <input checked="" type="checkbox"/> None reported
Type of auditors’ report issued on compliance for major programs:	Unqualified
Any audit findings disclosed that are required to be reported in accordance with Circular A-133, Section .510(a)?	Yes <input checked="" type="checkbox"/> No

Identification of major programs:

CFDA Number	Name of Federal Program or Cluster
14.228	Community Development Block Grant – State’s Program
14.871	Section 8 Housing Choice Voucher
93.600	Head Start Program
Dollar threshold used to distinguish between Type A and Type B programs	\$300,000
Auditee qualified as low-risk auditee?	Yes No <input checked="" type="checkbox"/>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

Section II – Financial Statements Findings

Finding Reference	04-01
Requirement	Financial Reporting – Accounting Records
Statement of Condition	During our examination of the Municipality's accounting system we noted that it does not summarize the transactions in a formal General Ledger in order to properly record and account for the transactions of all of its Governmental Funds (Local, State and Federal funds) and Account Groups.
Criteria	Chapter VII Article 8.010 of State Act Number 81 of August 30, 1991 states that the Municipality should maintain an effective and updated accounting system.
Cause of Condition	The Municipality did not establish effective internal control over the transactions recorded on its accounting records. Also, the accounting data is not summarized in the form of a double-entry general ledger record.
Effect of Condition	The Municipality accounting system did not provide updated and complete financial information that present the financial position and the result of operations and the change in fund balances. Such information is necessary to take management decisions.
Recommendation	We recommend that the Municipality should implement internal control and procedures in order to maintain an accounting system that contains information pertaining to authorizations, obligations, unobligated balances, assets, liabilities, outlays or expenditures, interfund transactions, etc.
Questioned Costs	None
Management Response and Corrective Action Plan	The Municipality Management concurs with the finding. Auditor's recommendation would be considered as part of corrective action plan development and implementation.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

Section II - Financial Statements Findings

Finding Reference	04-02
Requirement	Expenditures for Goods and Services and Account Payables - Purchasing and Receiving
Statement of Condition	<p>We performed a cash disbursement test and examined , thirty eight (38) disbursement vouchers related to CDBG Program and forty one (41) disbursement vouchers related to Head Start Program. The following will summarize the internal control exceptions noted:</p> <ul style="list-style-type: none">a. In twenty (20) cases related to CDBG Program, the Purchase Order was issued after the receipt of the goods and services.
Criteria	<p>The Revised Regulations on Basic Standards for the Municipalities of Puerto Rico establish in Chapter four (4) that the Finance Director will be responsible to account and to prepare disbursements through documents duly prepared and certified, including sufficient evidential matter to support the transactions. Chapter eight (8) of the Revised Regulations on Basic Standards for the Municipalities of Puerto Rico establishes the procedures related to the formal bids or quotations for the purchase of goods or services. Also, the Article 10.007 of State Act Number 81 of August 30, 1991 establishes procedures to request and obtain bids and quotation from the suppliers.</p>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

Section II - Financial Statements Findings

Finding Reference 04-02 (continued)

Cause of Condition The Municipality controls and procedures failed to assure that funds were committed before the acquisition of goods or services.

Effect of Condition The Municipality is not in compliance with Chapter four (4) and Chapter (8) of the Revised Regulations on Basic Standards for the Municipalities of Puerto Rico and with the State Act Number 81 of August 30, 1991.

Recommendation We recommend that the Municipality should strengthen internal control procedures to assure that the purchase order is issued before the acquisition of goods or services.

Questioned Cost None.

Management Response and Corrective Action Plan The Municipality Management concurs with the finding. Auditor's recommendation would be considered as part of corrective action plan development and implementation.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference	04-03
Program	Community Development Block Grant – State's Program (CFDA. No. 14.228); U.S. Department of Housing and Urban Development; Pass through State – Office of the Commissioner of Municipal Affairs (OCAM)
Requirement	Allowable Costs and Cost Principles
Statement of Condition	Section II – Financial Statement Findings – Finding Reference 04-02

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference	04-04
Program	Community Development Block Grant – State’s Program (CFDA No. 14.228); U.S. Department of Housing and Urban Development; Pass through State – Office of the Commissioner of Municipal Affairs (OCAM)
Requirement	Allowable Activities
Statement of Condition	During our examination of eight (8) participant files maintained by the Municipality, related to assistance for housing rehabilitation, we noted that the written policies and procedures adopted by the Municipality for Housing Rehabilitation Activities were not followed by the Program Staff as established in the Manual.
Criteria	24 CFR, Section 570.506 (b) state that at a minimum, the grantee should maintain records demonstrating that each activity undertaken meets one of the three national objectives of the CDBG Program, i.e., benefit low- and moderate-income persons, prevent or eliminate slums or blight, or meet community development needs having a particular urgency. Also, 24 CFR, Section 570.506 (b) (9) states that when CDBG- Entitlement Grant funds are used for residential rehabilitation activity to aid in the prevention or elimination of slums or blight in a slum or blighted area, the grantee must maintain records to support the local definition of “substandard”, must document a pre-rehabilitation inspection report describing the deficiencies in each structure to be rehabilitated, and must document the details and scope of CDBG assisted rehabilitation, by structure.
Cause of Condition	The Municipality’s internal controls procedures failed to assure that inspections to monitor the rehabilitation activities were conducted, as established in the contracts with the participants, by the program staff.
Effect of Condition	The Municipality is not in compliance with 24 CFR, Section 570.506 and with 24 CFR, Section 570.506 (b) (9).

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference 04-04 (continued)

Recommendation

We recommend the Program to establish the following procedures:

- a. Ascertain that the participant housing unit deficiencies to be corrected are incorporated into the rehabilitation contract.
- b. Realize pre-rehabilitation inspections describing the participant housing unit deficiencies to be corrected.
- c. Assign a staff to inspect the rehabilitation work upon completion to assure that is carried out in accordance with contracts specifications.
- d. Assure that all participant files include all required documentation, how family composition, residence existence.
- e. Ascertain eligibility determination and adequate evidence of family income.

Questioned Costs

None

**Management Response
and Corrective Action
Plan**

The Municipality Management concurs with the finding. The Program Director will give instructions to the program staff to follow the written instructions and procedures adopted in the Housing Rehabilitation Manual.

Responsible Person: Mr. Antonio Baez - Data Operator

Implementation date: May, 2005

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference	04-05
Program	Community Development Block Grant - State's Program (CFDA. No. 14.228); U.S. Department of Housing and Urban Development; Pass through State - Office of the Commissioner of Municipal Affairs (OCAM)
Requirement	Procurement and Suspension and Debarment
Statement of Condition	<p>During our contract provision test, we noted the following situations:</p> <ul style="list-style-type: none">a. Two (2) contracts did not include a provision for compliance with executive order "Equal Employment opportunity"b. Two (2) contracts did not include a provision for granting accesses to GAO or other federally agency, to books and other documents.c. Two (2) contracts did not include a provision for compliance with Energy Policy and Conservation Act.d. Two (2) contracts did not include a provision for compliance with the Copeland "Anti-Kickback".e. Two (2) contracts did not include provision for compliance with EO-1991-55.
Criteria	Code of Federal Regulations 24, Part 570.489 (g) requires that all purchase orders and contracts include any clauses required by Federal Statutes, executive orders and implementing regulations.
Cause of Condition	The Municipality did not maintain appropriate monitoring procedures to detect the exclusion of certain contract clauses.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference	04-05 (Continued)
Effect of Condition	The Municipality is not in compliance with Code of Federal Regulations 24, Part 570.489 (g).
Recommendation	We recommend management to update contract model according with the federal requirements.
Questioned Costs	None
Management Response and Corrective Action Plan	The Municipality Management concurs with the finding. The Program Director requested Ms. Carmen Escobar, Director of the Municipality's Secretary Office, information of the clauses required to be included in the Federal fund contracts. New contracts for the following fiscal year will contain all clauses requested by Federal Law.

Responsible Person: Carmen Escobar-Municipal Secretary Office Director

Implementation date: April, 2005

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

Section III – Mayor Federal Award Program Finding and Questioned Cost

Finding Reference	04-06
Program	Community Development Block Grant – State's Program (CFDA. No. 14.228); U.S. Department of Housing and Urban Development; Pass through State – Office of the Commissioner of Municipal Affairs (OCAM)
Requirement	Sub-recipient Monitoring
Statement of Condition	The Municipality disbursed CDBG funds to a sub-recipient and did not perform the necessary monitoring procedures to obtain a reasonable assurance that the sub-recipient administers program funds in compliance with Federal requirements.
Criteria	Code of Federal Regulations 24, Section 570.503 states that before disbursing any CDBG funds to a sub-recipient the Municipality should assure that the agreement between parties include provisions concerning: the statement of work, records and reports, program income and uniform administrative requirements. In addition, the Municipality must perform monitoring activities in order to review the financial information and observes that operations of the sub-recipients are realized in accordance with the agreement.
Cause of Condition	The Municipality controls and procedures failed to assure that sub-recipient comply with the program requirements.
Effect of Condition	The Municipality is not in compliance with Code of Federal Regulations 24, Section 570.503.
Recommendation	We recommend management to apply the required monitoring to the sub recipient using the following techniques: <ul style="list-style-type: none">a. Obtaining sub recipient single audit report, if applicable;b. Issuing timely management decisions for audits and monitoring findings to inform the sub recipient whether the corrective action plan is acceptable;c. Maintaining a system to track and follow-up on reported deficiencies related to programs funded the CDBG funds and ensure that timely corrective action is taken;

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference

04-06 (Continued)

- d. Reviewing sub recipient reports and following-up on areas of concern;
- e. Monitoring sub recipient budget;
- f. Performing site visit to sub recipient to review financial and programmatic records and observe operations.
- g. In the agreement include a provision concerning the statement of work, the program income requirement applicable to CDBG program, the uniform administrative requirements and the sub recipient the requirement to comply with the compliance requirements applicable to federal program, including the audit requirement of OMB A-133.

Questioned Costs

\$56,250

Management Response and
Corrective Action Plan

The Municipality Management concurs with the finding. Auditor's recommendation would be considered as part of corrective action plan development and implementation.

Responsible Person: Mr. Jorge Correa Bernier – Federal Program Director

Implementation date: June, 2005

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference	04-07 N/A
Program	Head Start (CFDA. No. 93.600); U.S. Department of Health and Human Services; Pass through Sate - Commonwealth of Puerto Rico Administration for Children and Families -ACUDEN
Requirement	Cash Management
Statement of Condition	During our Cash Management test, we noted that the Municipality requested funds that were not disbursed on a reasonable lapse of time. Also, a monthly average cash balance of \$42,257 was maintained during the fiscal year ended June 30, 2004.
Criteria	Code of Federal Regulations 45, Subpart C, Section 92.20 (b) (7) states that the Municipality must maintain procedures for minimizing the time elapsed between the transfer of funds from the U.S. Treasury and disbursement by grantees and sub grantees whenever advance payment procedures are used.
Cause of Condition	The cash advance procedures established by the Commonwealth of Puerto Rico Administration for Children and Families through grant agreement provide for only an advance per month.
Effect of Condition	The Municipality requested funds in excess of immediate needs and therefore, is not in compliance with Code of Federal Regulations 45, Subpart C, Section 92.20 (b) (7).
Recommendation	We recommend management to continue strengthen it's procedures to minimize the time elapsed between the transfer of funds from the Commonwealth of Puerto Rico Administration for Children and Families and the disbursements made by the Municipality.
Questioned Costs	None

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference 04-07 (Continued)

Management Response and The Municipality's Management concurs with the finding.
Corrective Action Plan Auditor's recommendation would be considered as part of
corrective action plan development and implementation.

Responsible Person: Mr. Nelson Medina, Director

Implementation date: March, 2005

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

Section III - Major Federal Award Program Findings and Questioned Costs

Finding Reference	04-08 N/A
Program	Head Start (CFDA. No. 93.600); U.S. Department of Health and Human Services; Pass through State - Commonwealth of Puerto Rico Administration for Children and Families- ACUDEN
Requirement	Matching, Level of Effort, Earmarking -Matching
Statement of Condition	<p>In our sample of fifteen (15) Participants Files, constituted by 90 percent of low income participants and which was realized to support our Earmarking Test, we noted the following exceptions:</p> <ul style="list-style-type: none">a. The program did not request to the applicants household a copy of the Social Security Card and Birth Certificate of all family members to assure participant family composition.b. In one (1) file, the participant was not correctly classified as a participant whose income family was above poverty guideline.
Criteria	CFR 45, Section 1305.4, establishes that at least 90 percent of enrollees must come from families whose income is below the Official Federal Poverty Guidelines or who are receiving public assistance.
Cause of Condition	The program internal control failed to assure that participants exceeding poverty guidelines are duly classified in that category.
Effect of Condition	In these cases, the program was not in compliance with 45 CFR Section 1305.4
Recommendation	We recommend that the Municipality should improve monitoring procedures to reduce the risk of noncompliance with this requirement.
Questioned Costs	None

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference

04-08 (Continued)

Management Response and
Corrective Action Plan

The Municipality's Management concurs with the finding. Auditor's recommendation would be considered as part of corrective action plan development and implementation.

Responsible Person: Mr. Nelson Medina, Director

Implementation date: March, 2005

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference	04-09 N/A
Program	Head Start (CFDA. No. 93.600); U.S. Department of Health and Human Services; Pass through State – Commonwealth of Puerto Rico Administration for Children and Families -ACUDEN
Requirement	Earmarking Test – 90%
Statement of Condition	The program did not comply with enrollment levels established by Head Start program. The participants enrolled with income above the official Federal Poverty Guidelines were exceeding the 12 percent.
Criteria	Code of Federal Regulations 45, Section 1305.4 (b) (1) establishes the highest percentage allowed to participants that come from high level income.
Cause of Condition	The program did not maintain appropriate procedures and internal control to assure the level stipulated for program regulation.
Effect of Condition	The program did not comply with the Code of Federal Regulations 45, Section 1305.4 (b) (1) because the participants enrolled with high incomes exceed the 10% stipulated federal regulation.
Recommendation	We recommend the Municipality should strengthen its control and procedures to assure that the level of participants admitted with income above the official federal poverty guidelines.
Questioned Costs	None
Management Response and Corrective Action Plan	The management concurs with our recommendation and expects to correct the situation as soon as possible. Auditor's recommendation would be considered as part of corrective action plan development and implementation.

Responsible Person: Mr. Nelson Medina, Director

Implementation date: March, 2005

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

Section III – Mayor Federal Award Program Findings and Questioned Costs

Finding Reference	04-10 N/A
Program	Head Start (CFDA. No. 93.600); U.S. Department of Health and Human Services; Pass through State – Commonwealth of Puerto Rico Administration for Children and Families-ACUDEN
Requirement	Matching, Level of Effort, Earmarking – Administrative Cost Limits
Statement of Condition	The Accounting System maintained by the Head Start Program financial activities did not provide for the classification of financial transactions between administration and programmatic costs. Alternate procedures were used by the Program staff to compute compliance with the fifteen percent (15%) administrative costs limit.
Criteria	Code of Federal Regulations 45, Subpart C, Section 92.20 (a) (2) states that the sub grantees must maintain fiscal controls and accounting procedures sufficient to permit the tracing of funds to a level of expenditures adequate to establish that such funds have not been used in violation of the restriction and prohibitions of applicable statutes.
Cause of Condition	The Municipality accounting records did not provide a chart of account to account by separate, programmatic and administrative expenditures.
Effect of Condition	Such condition may cause Municipality's non-compliance with certain compliance requirements like: allowable costs, activities allowed and unallowed; and earmarking.
Recommendation	We recommend management to modify the Accounting System chart of accounts to create separate accounts for administrative and programmatic expenditures. Also, cost with dual benefits (administrative and programmatic) should be identified and allocated appropriately using a cost-benefit proportion.
Questioned Costs	None

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

Section III – Mayor Federal Award Program Findings and Questioned Costs

Finding Reference 04-10 (Continued)

Management Response and The Municipality's Management concurs with the finding.
Corrective Action Plan Auditor's recommendation would be considered as part of
corrective action plan development and implementation

Responsible Person: Mr. Nelson Medina, Director

Implementation date: March, 2005

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference	04-11 N/A
Program	Head Start (CFDA. No. 93.600); U.S. Department of Health and Human Services; Pass through State – Commonwealth of Puerto Rico Administration for Children and Families -ACUDEN
Requirement	Reporting
Statement of Condition	<p>During our reporting test, whose samples were four (4) monthly reports, we noted the following exceptions:</p> <ul style="list-style-type: none">a. Two (2) monthly reports were not available for our examination.b. Two (2) monthly reports had no evidence that the report was submitted on time.c. One (1) monthly report was submitted subsequent to the deadline.d. Four (4) monthly reports did not agree with the amounts per accounting records.
Criteria	OBM Common Rules, Subpart C, 45 CFR 92.20 (b)(1), requires that accurate, current, and complete disclosure of the financial results of financially assisted activities must be made in accordance with the financial reporting requirements of the grant or sub-grant. Also, Subpart C, 45 CFR 92.20 (b) (2), states that the grantee must maintain records, which adequately identify the source and application of funds, provided for financially assisted activities.
Cause of Condition	The Municipality did not maintain adequate controls to assure a proper tracing of financial reports to the accounting records exist and timely submission of monthly reports.
Effect of Condition	The Municipality is not in compliance with Code of Federal Regulation 45, Subpart C, Section 92.20 (b) (1) and 92.20 (b) (2), provisions regarding financial reporting and did not comply with Federal Regulations that require the timely submission of the monthly reports.

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)

YEAR ENDED JUNE 30, 2004

Section III – Major Federal Award Program Findings and Questioned Costs

Finding Reference 04-11 (continued)
Program Head Start (CFDA. No. 93.600); U.S. Department of Health and Human Services; Pass through State – Commonwealth of Puerto Rico Administration for Children and Families -ACUDEN

Recommendation We recommend that the Municipality should establish internal controls and procedures in order to assure that financial reports are in accordance to the financial information detailed in the accounting records. Also, the reports must be prepared and submitted to ACUDEN in the required period.

Questioned Costs None

Management Response and Corrective Action Plan The Municipality's Management concurs with the finding. Auditor's recommendation would be considered as part of corrective action plan development and implementation

Responsible Person: Mr. Nelson Medina, Director

Implementation date: March, 2005

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA

SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS (CONTINUED)

YEAR ENDED JUNE 30, 2004

Original Finding Number	CFDA No.	Current Status of Prior Year Audit Federal Award Findings - Part III Findings (As required by OMB Circular A-133)
03-03	14.228	<p><u>Seven (7) CDBG Program disbursement vouchers did not have all supporting documents stamped as paid. Two (2) CDBG Program disbursement vouchers were not pre-numbered. One (1) CDBG Program disbursement voucher did not include the invoice. In one (1) CDBG Program disbursement voucher there was no evidence of receiving report or the certification of the Municipality's employee who received the goods or services. In nine (9) CDBG Program disbursement vouchers the purchase order were dated after the receiving report and invoice date.</u></p> <p>No corrective action has been taken. The auditors reissued the finding in the current year. See Finding Reference 04-03.</p>
03-04	14.228	<p><u>Three (3) housing rehabilitation participant files did not include the pre-rehabilitation inspection specifying which were the participant housing unit deficiencies to be corrected. Two (2) files did not include the birth certificate neither copy of the social security for the family members. Two (2) files did not include the residence deed neither utilities invoices as evidence of residence existence. In three (3) cases the eligibility determination was not properly documented.</u></p> <p>No corrective action has been taken. The auditors reissued the finding in the current year. See Finding Reference 04-04.</p>
03-05	14.228	<p><u>Three (3) contracts did not include a provision for granting access to GAO or other federally agency, to books and other documents. Three (3) contracts did not include a provision for compliance with the Clean Air Act and Water Act. Three (3) contracts did not include a provision for compliance with Energy Policy and Conservation Act. Three (3) contracts did not include a provision for compliance with the Copeland "Anti-Kickback". Three (3) contracts did not include a provision for retention of all required records for three years.</u></p> <p>No corrective action has been taken. The auditors reissued the finding in the current year. See Finding Reference 04-05.</p>
03-06	14.228	<p><u>The Municipality pass-through program funds to another entity and did not perform the necessary monitoring procedures to obtain a reasonable assurance that the sub recipient administers program funds in compliance</u></p>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA

SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS (CONTINUED)

YEAR ENDED JUNE 30, 2004

Original Finding Number	CFDA No.	Current Status of Prior Year Audit Federal Award Findings - Part III Findings (As required by OMB Circular A-133)
		<p><u>with Federal requirements.</u></p> <p>No corrective action has been taken. The auditors reissued the finding in the current year. See Finding Reference 04-06.</p>
03-07	14.228	<p><u>During the fiscal year 2002-2003, the Municipality maintained two Certificates of Deposits amounting \$ 72,988, which represents an activity not eligible under the CDBG State Program. Such Certificates of Deposit earned interests amounting \$ 246.19.</u></p> <p>Full corrective action has been taken..</p>
03-08	14.871	<p><u>Sixteen (16) Housing Voucher Program disbursement vouchers did not have all supporting documents stamped as paid. Thirteen (13) Housing Voucher Program disbursement vouchers did not include an approved and pre numbered purchase requisition. Four (4) Housing Voucher Program disbursement vouchers did not include the invoice. In two (2) Housing Voucher Program disbursement vouchers there was no evidence of receiving report or the certification of the Municipality's employee who received the goods or services. In four (4) Housing Voucher Program disbursement vouchers the purchase order were dated after the receiving report and invoice date.</u></p> <p>Full corrective action has been taken.</p>
03-09	14.871	<p><u>Six (6) participant's files did not include annually a release form to allow the PHA to obtain information from third parties. Six (6) participant's files did not include annually a release form to allow the PHA to obtain information about the employment. In six (6) participant's files there was no evidence that the PHA provide to the assistance applicants and to the participants in the annual income recertification a "Privacy Act Notice". Three (3) participant's files did not contain a release form to allow the PHA to obtain information form third parties, signed by the head of household spouse or by any members of the family composition who is at least eighteen (18) years of age. Two (2) participant's files did not include a federally prescribed general release form to allow the PHA to obtain information about the employment, signed by the head of household spouse or by any members of the family composition who is at least eighteen (18) years of age.</u></p>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA

SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS (CONTINUED)

YEAR ENDED JUNE 30, 2004

Original Finding Number	CFDA No.	Current Status of Prior Year Audit Federal Award Findings - Part III Findings (As required by OMB Circular A-133)
		Full corrective action has been taken.
03-10	14.871	<u>The determination of reasonable rent (reasonable rent certification) was not duly documented in thirteen (13) participant files examined. The certification included only one comparable unassisted unit to determine that the rent to owner is reasonable.</u>
		Full corrective action has been taken.
03-11	14.871	<u>Newspaper publication informing to the public that a new waiting list was prepared during the fiscal year 2002-2003 was not available for our examination.</u>
		Full corrective action has been taken.
03-12	14.871	<u>The Municipality maintained during the current fiscal year average cash balance in books of approximately \$226,484. At June 30, 2003, the cash balance in book was \$234,090; \$43,734 of these funds was from HUD overpayment during the fiscal year 2002-03 as determined in the year-end settlement; \$57,063 was from operating reserve at June 30, 2003, as determined in the year-end settlement; and the remaining \$133,293 was not identified by us with respects to its origin.</u>
		Full corrective action has been taken.
03-13	93.600	<u>Three (3) Head Start Program cancelled checks were not available for our examination. One (1) Head Start disbursement vouchers did not have all supporting documents stamped as paid. In two (2) Head Start disbursement vouchers we did not have evidence about if three (3) quotations were requested and obtained prior to order the goods or services, or prior to contract date.</u>
		Full corrective action has been taken.
03-14	93.600	<u>The Municipality requested funds that were not disbursed on a reasonable lapse of time. Also, a monthly average cash balance of \$88,191 was maintained during the fiscal year ended June 30, 2003.</u>

COMMONWEALTH OF PUERTO RICO
MUNICIPALITY OF GUAYAMA

SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS (CONTINUED)

YEAR ENDED JUNE 30, 2004

Original Finding Number	CFDA No.	Current Status of Prior Year Audit Federal Award Findings - Part III Findings (As required by OMB Circular A-133)
		No corrective action has been taken. The auditors reissued the finding in the current year. See Finding Reference 04-07.
03-15	93.600	<u>The Accounting System kept by the Head Start Program did not provide for the classification of financial transactions between administration and programmatic costs. Alternate procedures were used by the Program staff to compute compliance with the fifteen percentage (15%) administrative costs limit.</u>
		No corrective action has been taken. The auditors reissued the finding in the current year. See Finding Reference 04-10.
03-16	93.600	<u>Some differences between the amounts of the in-kind contribution registered in the General Ledger and the supporting documents for the in-kind contribution were observed for the months of October, 2002, and February, 2003. Also, the Municipality included in their Local In-Kind Contribution the salary and fringe benefits costs of some municipal employees, which were not providing service to the Program during the audit period due to resignation or license without compensation.</u>
		Full corrective action has been taken.
03-17	93.600	<u>In two (2) Centers the Fire Department license was expired. In three (3) Centers the Fire Department license presented deficiencies in the Fire Department Inspection Checklist. At the date of February 29, 2004 they did not have Fire Department license. Also, in one (1) case the Center presented Fire Department Inspection Checklist without deficiencies, but the license was not available for our examination. In four (4) Centers the Health Department license presented were pending because deficiencies were noted by the Health Department inspectors during his inspections.</u>
		Full corrective action has been taken.
02-04	14.228	<u>The Municipality should apply monitoring procedures, including obtaining contractor's and if applicable subcontractor's weekly payrolls to be reviewed weekly by responsible municipal employee.</u>
		Full corrective action has been taken.

COMMONWEALTH OF PUERTO RICO
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SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS (CONTINUED)

YEAR ENDED JUNE 30, 2004

Original Finding Number	CFDA No.	Current Status of Prior Year Audit Federal Award Findings - Part III Findings (As required by OMB Circular A-133)
02-05	14.228	<p><u>The Municipality should maintain its cash management internal control procedures to assure compliance with the cash management requirement.</u></p> <p>Full corrective action was taken.</p>
02-06	14.228	<p><u>The Municipality should implement procedures in order to assure the proper valuation and timeliness of recognition of real property and equipment as well as Construction in progress in the Property Subsidiary Ledger in a manner that it provides updated and complete financial information. The employee in charge of Municipal Property should maintain daily communication with the Purchase Department of the Municipality and with the Federal Programs employee in charge of the property and equipment in order to assure that all property and equipment acquired during the year is properly recorded in the subsidiary ledger.</u></p> <p>Full corrective action has been taken.</p>
02-07	14.228	<p><u>The Municipality should update contract model according with the federal requirements.</u></p> <p>No corrective action has been taken. The auditors reissued the finding in the current year. See Finding Reference 04-05.</p>
02-08	14.228	<p><u>The Municipality should strengthen its procedures to assure that all disbursements vouchers contain all supporting documents and approval signatures before the related payments are made.</u></p> <p>No corrective action has been taken. The auditors reissued the finding in the current year. See Finding Reference 04-03.</p>
02-09	14.228	<p><u>The Municipality should properly document the procedures followed in the evaluation of the proposals and in the final determination. The Municipality should implement a checklist to be used for each auction file to assure the completeness of the required documentation.</u></p> <p>Full corrective action has been taken.</p>
02-10	93.600	<p><u>The Municipality should strengthen its procedures to assure that all disbursements vouchers contain all supporting documents and approval</u></p>

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SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS (CONTINUED)

YEAR ENDED JUNE 30, 2004

Original Finding Number	CFDA No.	Current Status of Prior Year Audit Federal Award Findings - Part III Findings (As required by OMB Circular A-133)
		<u>signatures before the check issuance.</u>
		Full corrective action has been taken.
02-11	93.600	<u>On a monthly basis the Human Resources Department should send to the Head Start Program a written certification stating the salary and fringe benefits of each municipal employee that provide services to the Head Start Program. Also, the Municipality should implement controls and procedures in order to assure accurate accounting records are maintained and current and complete disclosure of financial results are presented in the financial reports. Also, the Municipality should implement procedures in order to assure that the contribution will be recorded at fair market value of the supplies at the time of donation.</u>
		Full corrective action has been taken.
02-12	93.600	<u>The Municipality should continue to strengthen it's procedures to minimize the time elapsed between the transfer of funds from the Administration for Children and Families and the disbursements made by the Municipality.</u>
		No corrective action has been taken. The auditors reissued the finding in the current year. See Finding Reference 04-07.
02-13	93.600	<u>The Municipality should follow monitoring system procedures developed, including obtaining contractor's and subcontractors weekly payrolls to be reviewed weekly by responsible Municipal Employee. Also, interview contractor's and subcontractor's laborers periodically (up to ten percent (10%) of the workers on long term projects) in order to establish the degree of compliance and the nature and extend of violations, if any.</u>
		Full corrective action has been taken.
02-14	93.600	<u>The Municipality should modify the Head Start program accounting system chart of accounts in order to create separate accounts for administrative and programmatic expenditures. Also, cost with dual benefits (administrative and programmatic) should be identified and allocated appropriately using a cost-benefit proportion.</u>

COMMONWEALTH OF PUERTO RICO
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SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS (CONTINUED)

YEAR ENDED JUNE 30, 2004

Original Finding Number	CFDA No.	Current Status of Prior Year Audit Federal Award Findings - Part III Findings (As required by OMB Circular A-133)
		No corrective action has been taken. The auditors reissued the finding in the current year. See Finding Reference 04-10.
02-15	93.600	<u>The Municipality should implement internal control procedures in order to maintain adequate and accurate accounting records.</u> Full corrective action has been taken.
02-16	93.600	<u>The Municipality should establish routine visits to the different centers in order to assure that the centers are in very good conditions. Such conditions are necessary to comply with the licensing requirement. We also recommend that the Municipality should review the Centers files to assure completeness of the required documentation and perform periodically follow-up procedures in order to update such files.</u> Full corrective action has been taken.
02-17	14.871	<u>The Municipality should establish monitoring procedures to assure that all participant's files include all documentation required by federal agencies.</u> Full corrective action has been taken.
02-18	14.871	<u>The Municipality should establish adequate controls to assure that the rent paid to the owners was reasonable.</u> Full corrective action has been taken.
02-19	14.871	<u>The Municipality should improve monitoring procedures to assure that the exceptions detailed in the inspection reports are duly corrected by the owner or the participant in the required period.</u> Full corrective action has been taken.
02-20	14.871	<u>The Municipality should improve internal controls and monitoring procedures to assure that the program comply with federal regulations.</u> Full corrective action has been taken.
02-21	14.871	<u>The Municipality should evaluate utility allowance rate each year as</u>

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SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS (CONTINUED)

YEAR ENDED JUNE 30, 2004

Original Finding Number	CFDA No.	Current Status of Prior Year Audit Federal Award Findings - Part III Findings (As required by OMB Circular A-133)
		<u>established in the federal regulations.</u>
		Full corrective action has been taken.
02-22	14.871	<u>The Municipality should strengthen it's procedures to minimize the time elapsed between the transfer of funds from the federal agency and the disbursements made by the Municipality.</u>
		Full corrective action was taken.
01-05	14.228	<u>The Municipality did not apply adequately the monitoring system developed to ensure contractors compliance with payment of prevailing wages rates to employees</u>
		Audit finding is no longer valid since has passed more than two years since the reports were submitted to the Single Audit Clearinghouse. The Federal Agency who delegated the funds to the Municipality is not giving follow up to the finding and has not issued a final decision respect to the finding.
01-07	14.228	<u>Contracts without required clauses</u>
		Audit finding is no longer valid since has passed more than two years since the reports were submitted to the Single Audit Clearinghouse. The Federal Agency who delegated the funds to the Municipality is not giving follow up to the finding and has not issued a final decision respect to the finding.
01-09	93.600	<u>Unallowable matching share costs recorded</u>
		Audit finding is no longer valid since has passed more than two years since the reports were submitted to the Single Audit Clearinghouse. The Federal Agency who delegated the funds to the Municipality is not giving follow up to the finding and has not issued a final decision respect to the finding.
01-11	93.600	<u>Centers operating without licenses required</u>
		Audit finding is no longer valid since has passed more than two years since the reports were submitted to the Single Audit Clearinghouse. The Federal Agency who delegated the funds to the Municipality is not giving follow up to the finding and has not issued a final decision respect to the finding.

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SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS (CONTINUED)

YEAR ENDED JUNE 30, 2004

Original Finding Number	CFDA No.	Current Status of Prior Year Audit Federal Award Findings - Part III Findings (As required by OMB Circular A-133)
01-12	14.228	<u>No appropriate documentation on auction files</u>
Audit finding is no longer valid since has passed more than two years since the reports were submitted to the Single Audit Clearinghouse. The Federal Agency who delegated the funds to the Municipality is not giving follow up to the finding and has not issued a final decision respect to the finding.		